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EVERYBODY'S LEGAL ADVISER

Everybody's Legal Adviser

Volume IV

The Law of Shipping; Marine Insurance; Fire Insurance; Life and Accident Insurance; Mortgage of Personal Property; Pledge of Personal Property; Rights of Lienors; Innkeepers; Warehousemen; Bailors and Bailees; Trustees; Executors; Administrators; Corporations; Directors; Stockholders

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CHAPTER XIX

SHIPPING

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1. A SHIP is personal property, and her ownership and transfer are regarded in this country by rules similar, in some respects, to those that apply to real property. The Federal Constitution authorised Congress to enact laws for regulating commerce. Accordingly, in 1792 an act was passed for registering the names of the owners of ships and for navigating them.

2. By this act an American vessel may be registered in the custom house. The law does not say that this must be done, but the disadvantage of not complying is so great that all vessels are registered. The ships

that may be registered are those built within the United States, and owned wholly by citizens, as well as some others that need not be mentioned. No ship can be registered whose owner, or part owner, resides abroad, although he is a citizen, unless he is a consul of the United States, and an agent for, or partner in, an American mercantile house. The master must also be a citizen of the United States. The law also declares that a vessel whose owner, or part owner, is a naturalised citizen and resides in the country whence he came more than a year, or in any foreign country more than two years, cannot be registered unless he is a consul or public agent of the United States. But a ship that has lost the benefits of registry by the non-residence of an owner may be registered anew if she becomes the property of a resident citizen by actual purchase.

Registration may be either permanent or temporary, but a vessel cannot have more than one register at the same time, and the temporary register is superseded by the permanent.

By enrolment is meant the registration of a vessel engaged in coastwise or inland navigation or commerce; and the same requirements must be observed as in the registration of vessels employed in foreign commerce. A license is similar to an enrolment, but is applied to vessels of less than twenty tons. The sale of a licensed vessel is not void, but if sold to a foreigner she is liable to forfeiture unless the owner had previously surrendered his license.

3. Sometimes Congress by special acts permits the

registration of a vessel as an American ship that has become so by purchase. The certificate of a registered American vessel that has been sold or transferred must be delivered up, or the vessel is forfeited. As soon as a registered vessel arrives from a foreign port her documents relating to ownership, freights, etc., must be deposited with the Collector of the Port to which she has come, and the owner or master must take oath that the register contains the names of all persons who are then owners of the ship, and at the same time report any transfer that has been made within his knowledge since the registry was made, and also declare that no foreigner has any interest in the ship. A register issued fraudulently, or with the knowledge of the owners, for a ship that was not entitled to one, would be void and the ship would be forfeited. After the issue of a new register the former must be surrendered. If a ship is transferred while at sea the old register must also be given up, and all the requirements of law concerning registry must be fulfilled within three days after her arrival at the home port.

4. Exclusive privileges at various times have been granted to registered vessels of the United States. A ship that is not registered nor licensed can sail on no voyage with the national protection. If she engages in foreign, or coasting trade, or fisheries, she may be forfeited, and if she has foreign goods on board, must also pay the tonnage duties that are levied on foreign ships. It may be remarked that every ship engaged in honest business, belonging to a civil-

ised people, has regular papers showing her nationality, unless they have been accidentally lost.

5. The statute relating to registration also provides how a vessel may be transferred. Whenever a sale or transfer is made there must be an instrument in writing of the nature of a bill of sale. A mere oral transfer, even though there was a valuable consideration, followed by possession, would give the transferee no right to claim a new registry setting forth his ownership. By a statute passed in 1850 no bill of sale or other conveyance is valid, or affects any person except the seller, unless it is recorded in the office of the collector of customs where the vessel is registered or enrolled. As a ship is personal property, the transfer should be accompanied by delivery of possession. Actual delivery is impossible where a ship is at sea. In such a case possession should be taken as soon as possible.

As between the parties the sale and delivery of a vessel suffices at common law to pass the title without a bill of sale unless the contract provides otherwise. By statute in England and Canada and some of the states a bill bill of sale is required.

The bill of sale entirely immediately divests the vendor of the title, and the vendee becomes entitled to all the benefits of ownership and assumes all the concurrent liabilities. The purchaser is not liable for repairs made and supplies furnished before the sale unless by special agreement, or unless the vessel was at sea at the time of the sale.

The sale of a vessel to a foreigner denationalises

her and deprives her of registry. By a sale to an American citizen her registry is lost, but she may be re-registered on proof of his citizenship. On arriving at a foreign port for business the master of a vessel must deposit the ship's register with the consul, or consular agent.

6. By the word ship, and still more by the phrase, ship and her appurtenances, or apparel, or furniture, everything passes connected with a ship and that is on board of or fastened to her needed for her navigation or for her safety.

7. The title to a ship may also be acquired by building. Under a contract for building an entire vessel, no property is in the party for whom she is built until delivery and acceptance, though circumstances may change the rule. Thus payment of the purchase price in installments as the work progressed, and construction under the superintendance of an agent who was authorised to approve or reject materials for the work, were not regarded as evidence of intention that the property in the vessel shall pass to the purchaser before delivery.

8. Two or more persons may become part owners of a ship in either of three ways. They may unite in building her, may join in purchasing her, or each may purchase his share independently of the others; in either case their rights and obligations are the same. If the register does not designate the proportions owned by each one, they are presumed to own the ship in equal shares.

9. A partnership relation is not to be inferred from

part ownership. If existing at all, it is by virtue of an agreement expressed or implied; it cannot be implied from the ownership of several persons of the same vessel. They are therefore tenants in common, and not partners.

10. Though individuals are simply part owners or tenants in common in the ownership of a vessel, they may be partners in employing her. When thus united as a partnership in employing her, they are liable as partners to third persons, and the earnings of the vessel are partnership funds. Whether the partnership between the part owners in employing the vessel is a continuing one, covering all voyages, or is restricted to a particular venture, is a question of fact to be determined by proper inquiry.

11. A majority of the owners may generally manage and direct how the vessel shall be employed. But as a ship is built to plough the sea, and not to lie by the wharf, there are certain positive rules relating to her employment. The employment of the ship is not, like the employment of a horse or other chattel, considered a matter of private concern alone, but through state action minority part owners may keep her employed against the wish of other part owners not so desiring. Such action is founded on the idea that the employment of a ship is a matter of public concern and interest.

But when the majority in interest desire to employ the vessel in a particular way, they may prevail against the wish of the minority. In a well-considered case the court declared that "if the minority happen to

have possession of the ship, and refuse to employ it, the majority may, by warrant for that purpose, obtain possession of the ship and send it to sea. upon giving the customary security to the minority for its safe return."

12. Again, suppose the owners are equally divided with respect to the employment of the vessel, who shall control? When the question is one of employment or non-employment, the party desiring its employment is entitled to possession and control, but when the conflict is over the question of the mode of employment, a court will not undertake to decide on the merits of the controversy, and award possession of the vessel to one party or the other. If they cannot decide among themselves the only remedy is to sell the vessel, and this, on a proper application to an admiralty court, will be ordered. "The tendency," says a recent writer of the courts, "is to confine the power of sale to cases where the warring interests are equal, both desirous of employing the vessel, and where, therefore, the ordinary rules as to the control in the case of disagreeing part owners would give the control to neither, and the effect of denying a sale would be to keep the vessel in idleness."

An owner of an unequal moiety of a vessel may be restrained by injunction from employing the vessel contrary to the wish of the other owners, but an injunction will not lie to restrain the majority from running the ship when they have given a bond to account for the share of the minority owners; and an injunction will be denied when a ship is about to

sail unless good reason is shown for the delay in making the application.

13. A tenant in common who has possession of a chattel may use it for his exclusive benefit, and likewise is liable for all charges affecting it. Though part owners of a vessel are tenants in common, the rule is modified in its application to them. Each part owner is entitled to receive his share of the earnings of the vessel unless he dissented from the voyage. The majority of part owners, therefore, cannot by excluding the minority from the possession of the vessel, deprive them of the proportion of the vessel's earnings. But a part owner who deserts from a proposed adventure absolves himself from the risk of loss and cuts himself off from sharing in the gains.

14. A part owner can transfer his interest without giving a notice to or obtaining the consent of the others. On the other hand, part owners, however numerous or large their interest, cannot by sale or mortgage affect the title of any opposing co-owner to his share in the vessel.

On his death his interest goes to his representative, and not to the other part owners.

15. The ship's husband, as he is called, is the agent of all the owners for the management of the ship, and is usually a part owner. He may be appointed by writing or otherwise. His duty is to provide for equipping and repairing the ship and taking care of her while in port. He also furnishes all regular and proper papers and makes contracts for freight or passengers, collects the receipts and pays the debts.

He cannot, without special authority, insure the ship for the other owners, nor buy a cargo, nor borrow money, nor give up a lien on the cargo for the freight, nor authorise someone else to do these things for him.

16. When he does not exceed his authority he binds the other part owners, but a third person may deal with him on his personal credit. And if they, believing he has thus dealt with a third person, settle their accounts with him, they are not liable to the creditor. He cannot establish a claim against them. To a ship's husband who is not a part owner every part owner is liable for the whole amount.

17. A ship is sometimes pledged as security for money borrowed. This contract is called bottomry. The essential features are: first, that the ship is bound for the payment of money; second, that it is to be repaid only in the event that the ship performs a certain voyage and arrives at the end in safety. Therefore, if a ship is previously lost, or before the expiration of the period specified, no part of the money is due; in other language, the whole debt is paid by the loss. As the lender thus consents that the repayment of the money shall depend on the safety of the ship, he has a right to charge an additional amount to the legal interest in order to cover his risk. This is called marine interest.

The loan may be for repairs, supplies to enable the ship to leave port; to free the ship from arrest; to unload the outward cargo; to meet the consul's charges and the like. A charge for commission in

procuring the loan is incidental to the loan itself.

18. A contract, whereby the lender takes more than legal interest, and is to be repaid, notwithstanding the loss of the ship, is not one of bottomry, and is illegal. But the lender may take marine interest and security for his debt in addition to the ship itself, in order to make the payment more sure on the arrival of the ship, provided that no payment is to be made in the event of her loss.

19. The most common contracts of bottomry are made by a master in a foreign port when money is needed and cannot otherwise be obtained. Sometimes they are nothing more than contrivances to get a large rate of interest. If the money is payable at the end of the voyage and the owner or master terminates the voyage sooner, either honestly or from a change of plans, or dishonestly by wrecking, or in some other way destroying the ship, the money is at once due.

20. When interest is not mentioned in the contract it will generally be regarded as included in the principal.

21. The rights and duties of the ship-owner and of the shipper are stated in an instrument called a bill of lading. This is a very ancient document, used by all commercial nations. It contains the names of the consignor, of the consignee, of the vessel, of the master, of the place of departure and of destination; also the price of the freight and other charges, and a sufficient description of the goods to indicate what they are. It is signed by the master of the ship. He ought not to sign it until the goods are actually on board,

but very often this is done before. Usually, a copy is retained by the master and three copies are given to the shipper, one of which he retains, another is sent to the consignee with the goods, while the third is sent to him in a different way.

22. The delivery is to the consignee or his assigns; in other words, to him or to such person as he may direct. This direction may be made by indorsing the bill and ordering the delivery of the goods to another; or the consignee may indorse the bill in blank, and whenever this is done any person who acquires an honest title thereto may write over the signature an order of delivery to himself. It is said that the consignee has this power to assign the bill even if the word assigns be omitted. As the indorsement transfers the property in the goods, the indorsee has a right to demand them. But on the non-delivery of the goods an action on the bill must be brought in the name of the original consignee.

23. As the bill of lading is evidence against the ship-owner that the goods have been received, and also of their quantity and quality, it is common to say "contents unknown," or "said to contain." Even without such words the bill of lading is not absolutely binding on the ship-owner, and he may, therefore, show that its statements were erroneous, either intentionally or by mistake.

24. The ship-owner has a lien on the goods for the freight money. The word freight is used in different senses. Sometimes it means the goods or cargo carried; sometimes the money paid by the shipper to

the owner for carrying them. When the term is used in this latter sense the word money is often added, "freight money," which leaves no question concerning what is meant.

25. The master cannot demand freight money without delivering the goods or offering to do so at the proper time, in the proper way, to the right person. After doing this the consignee is not entitled to the goods without paying the freight money due on them. This lien is established by law whether it is mentioned in the bill of lading or not.

26. By the common law an agreement to deliver goods before paying the freight money for carrying them destroys the lien. But, unless the ship owner intended to give up his security on the goods, it is said that a court would be inclined to preserve the master's security on the goods for a reasonable time, unless they should actually become the property of another by purchasing them.

27. The contract for carrying goods is for carrying the whole of them to the place of destination. Were a ship wrecked and the voyage not completed, there would be no right to recover compensation. But if a wreck or other accident happens, the master has the right to put them in another vessel and send them forward to their destination, and on their arrival he may claim the whole freight money. He not only may, but must send forward the goods at his own cost if he can do this by any reasonable means. He is not responsible, however, for any delay thus occurring.

28. The shipper, by his agent, may always recover his goods at any intermediate place by tendering all the freight money, because the master's right of sending them forward is merely to earn this. On the other hand, as the master cannot be deprived of his right to send them forward unless the shipper pays all the freight money, he must do this whenever he desires to obtain possession of his goods, however greatly they may be injured.

29. There are cases in which freight money is payable for a part of the distance, or to a certain degree, and the question is somewhat difficult, by what rule or proportion shall the freight money be measured? One rule is purely geographical and was formerly much used. That is, the whole freight money is payable for so many miles, and for a shorter distance in proportion. Another is of a purely commercial character. As the freight money is a fixed sum for the whole distance, what will it cost to bring goods to the place where they were received, and how much to take them to their original destination? Either of these rules has been generally adopted in this country.

30. A bill of lading requires delivery to the consignee or his assigns, "he or them paying freight," being the usual form. If the master delivers the goods without receiving the freight money he cannot fall back on the consignor and make him liable without showing that he actually owned the goods. Generally, the one who receives them is liable for the freight money; but he is not if merely an indorsee or assignee

of the consignee and obtains them by his order. If the master delivers goods to anyone, saying that he will look to him for the freight money, he may demand this of him, unless that person had the absolute right to them without paying it. This is rarely the case.

31. If freight money is paid in advance, and is not afterward earned, it must be repaid, unless the master can show that the owner took a less sum than he would otherwise have taken, and for this or some other reason the money paid was in final settlement, and was to be retained by the owner at all events.

32. Again, should a consignee pay too much, he may recover the excess, if it was paid through ignorance, or mistake; but he cannot do this if the payment were made with the full knowledge of all the facts, and his ignorance or mistake was simply concerning the law.

33. One who sells his ship after the beginning of a voyage can claim the freight money of the shipper, although the contract of sale may require him to pay it over to the purchaser. The mortgagee of a ship—that is, a person who has lent money on such security, who has not taken possession—has in general no right to the freight money, unless by a special agreement.

34. No freight money can be earned by an illegal voyage, as the law will not sanction or enforce an illegal contract. Goods are to be delivered by the bill of lading, in good condition, excepting the danger of seas and such other risks as may be mentioned. Yet

freight money is payable on goods injured by any of these perils yet actually delivered.

A shipper or consignee cannot abandon goods for the purpose of escaping payment of the freight money due on them, though they may be worthless, whenever their changed condition was caused by a sea risk. But if they are actually lost, though not in form, for example, if sugar has washed out of boxes or hogsheads, or wine has leaked out of casks in consequence of injuries arising from the perils of the sea a delivery of the boxes or casks without their contents is not a delivery of the sugar or wine, and consequently no freight money is due. For goods that are injured, or that actually perish, freight money must be paid.

On the other hand, a loss in consequence of the fault of the owner, the master or crew, must be made good.

35. The liability of shippers for carrying goods has been modified from time to time by federal statutes. The act of 1851 changed the fire risk of the owners of ships, but the act of 1893, known as the Harter act, wrought still more important changes. The purpose of the law is to require the owner to take the care of experts in that business in all matters relating to the loading, stowage, custody, care and proper delivery of the goods entrusted to him; also he must exercise due diligence to render the vessel seaworthy in all respects. Meeting all these requiremnts fully, neither the vessel nor her owners are responsible even for faults or errors in navigation, nor for such acci-

dents as have been legally put outside the pale of liability in bills of lading.

The greatest controversy in applying the act has been over the third section relating to seaworthiness. This does not relieve the owner from the duty of furnishing a seaworthy vessel at the beginning of the voyage, or affect his liability for damages to the cargo arising from unseaworthiness, but only exempts him from liability for damage arising from the risk therein designated when due diligence has been used to make the vessel seaworthy. The section does not relieve a vessel from liability for loss of cargo resulting from the gross fault or negligence of the master on showing that the owner had no knowledge or reason to believe that he was incompetent.

To constitute "due diligence" on the part of the ship owner to make the vessel in all respects seaworthy at the beginning of a voyage and thus entitle him to the benefit of the exemption, it is not sufficient to provide her with proper equipment; due diligence must be exercised by the owner's servants in using it, also in inspecting and repairing the ship, and the owner cannot escape if lacking in these regards, but only in latent defects that cannot be discovered by the utmost diligence.

36. The rules relating to passage are quite the same as those relating to the payment of freight money. Usually this is paid in advance. But it is not earned except by carrying the passenger, all or a portion of the way. If it is paid in advance and not earned

through the fault of the shipper or owner, it can be recovered.

37. The owner may let his ship, and this is done by an instrument called a charter-party. This agreement is of a variable nature depending on the circumstances and pleasure of the parties. Generally, only the right to carry goods is let; in legal phrase, the burden of the ship. The owner holds the possession of her, pays her master and crew and furnishes supplies and makes repairs and navigates her. Sometimes he lets his ship as he might let a house, and then the hirer takes possession, mans, navigates, supplies and even repairs her.

On thus letting a ship, if the hirer takes possession he gives bills of lading to the shippers of goods; if the ship owner retains possession, which is far more common, bills of lading are usually given by him as in the case of a general ship.

38. The charter-party designates the ship and master and parties, also her tonnage, or capacity; also what parts of the ship are let and what parts, if any, are reserved to the owner or to the master. It also describes the voyage or period of time for which the ship is hired, the days for remaining in port, the length of time for discharging the cargo, the obligation to man, navigate, supply and repair the ship, and all other particulars of the bargain. Finally, it states how much is to be paid for the ship, whether by the ton or otherwise, or a gross sum, for the whole burden, and when the money is payable and how, in what currency or in what exchange, especially if it is to

be paid abroad. Nor can the terms of the instrument be varied or changed by external evidence.

39. A hirer who takes the whole vessel pays for the whole, whether he fills her or not. Payment for the empty portion is said to be for dead freight. Either party who is deceived or defrauded by any statement in the charter-party can recover for the injury.

40. The voyage may be double; a voyage out and another in return, or a voyage to one port and then to another. The question sometimes arises whether any freight money is payable if the ship arrives in safety and delivers her cargo there and is lost on her return with the cargo she is then carrying. Of course, the parties may make what bargain they please, but when none is made the tendency of the courts is to consider each voyage at the end of which goods are delivered as a voyage by itself and earning its own freight money.

41. As time has become of the utmost importance in commercial transactions, both parties to the contract should be punctual and cause no unnecessary delay; for this without excuse, the party injured has a remedy against the other. The charter-party usually provides for so many lay-days, or working days, for loading or unloading the vessel. These are counted from her arrival at a wharf or other place of discharge, and not from her arrival at the port of destination. Sundays are computed in calculating lay-days at the port of discharge, but if the contract specifies working lay-days, Sundays and holidays are excluded.

If more than the agreed lay-days are occupied payment must be made for them, and demurrage means the sum which is thus paid. Usually the charterer agrees to pay a fixed sum as demurrage for each day. If after the lay-days allowed for unloading have begun, but before the cargo is unloaded, the ship and cargo, or cargo alone, without the fault of the owner or master, is lost, the freight money is due, because that was earned as soon as the vessel arrived. If time is occupied in repairing the ship without the fault of the owner or master, the charterer pays during this time, unless the repairs are in consequence of her original unseaworthy character.

One who charters a vessel under a contract that fixes no time for unloading and discharge impliedly contracts that he will unload and discharge her within a reasonable time. What this is, varies with the facilities of the port for discharging and other circumstances. It is the duty of the charterer or consignee, as the case may be, to designate and provide a suitable wharf or berth for the vessel within a reasonable time after her arrival, and is liable for the delay, but when he has fulfilled his obligation, the master of the vessel should proceed to the place designated. The charterer or consignee is not liable for delay caused by the crowded condition of the dock or because the vessel is compelled to wait its turn, especially if such waiting is required by the custom of the port. Demurrage is also reasonable for the detention of a vessel after loading and before unloading which is not due to the fault of the mas-

ter, such as a failure of the charterer to procure clearance papers. On the completion of the unloading the liability of the consignee or charterer for demurrage terminates, and he is not responsible for subsequent detention of the vessel.

42. Many cases have arisen in which the ship was delayed from different causes, giving rise to the question, which party ought to pay for the time thus lost? An eminent writer has said that no delay arising from the elements, as from ice or tides or tempests, or from any act of government, or from any disability of the consignee which could not be imputed to his own act, or to his own wrongful neglect, can give rise to a claim for demurrage. It is essentially due only for the fault or voluntary act of the charterer; but if a vessel is hired by the day, week or month, and is delayed by seizure, capture or other cause, and the impediment is removed and the ship completes her voyage, the charterer pays for the whole time. If she is condemned or otherwise lost this ends the voyage and the contract.

43. The contract may be dissolved by the parties or against their consent by any circumstance making its fulfilment illegal; for example, by a declaration of war on the part of the country to which the ship belongs against the country to which she was bound.

44. Next may be considered the navigation of the vessel. This is done by the master who is appointed by the part owners or a majority in interest of them. He has the whole care and supreme command of his vessel. He must see to everything relating to her

condition, including repairs, supplies, loading and unloading and navigating her. He is principally the agent of the owner; to some extent, however, he is the agent of the shipper, of the insurer, and also of all who are interested in the property under his charge.

45. Much of his authority as agent of the owner springs from necessity. Consequently, if the owner is present, or his agent, or is within easy reach, the master has no power to do many things which otherwise are within his authority.

(*a*) Thus, he can sell a ship only in a case of extreme necessity; in other words, only when it seems impossible to save her, and a sale is the only mode of preserving any part of her value for the owners or insurers. So, too, he can pledge her, but the necessity must be very great, though less than is required to authorise a sale. If money is really needed for the safety of the ship, and cannot be otherwise raised or not without great waste, a pledge can be made.

(*b*) Again, he cannot charter the ship unless a necessity exists. Of course, he can do this if he is clothed with the power; but when he does not possess it the necessity for doing so is simply a mercantile one and no other.

(*c*) Again, to bind the owner for repairs or supplies, there must be a necessity for them, but he is justified in incurring the expense if the condition of the vessel requires them for the safe and comfortable prosecution of the voyage.

(*d*) A master, unlike other agents, may substitute

another for himself who possesses all his authority whenever he is unable to discharge all his duties.

A master forfeits his right to wages whenever he is guilty of negligence or misconduct which results in serious damage or loss to the owners. But, if the negligence or misconduct does not cause injury or inconvenience to the owners, it does not effect a forfeiture of his wages, though the owner may be entitled to deduct or offset the damages actually sustained against the wages due to him. Nor will he incur the penalty of a forfeiture of his wages by a mere error of his judgment, although it results in a loss. Habitual intoxication of the master will effect a forfeiture of his wages, but occasional acts of this kind, if unaccompanied with neglect of duty, will not have that effect. A master's wages may also be forfeited by desertion.

(*e*) As the majority of the part owners can appoint the master, so can they remove him. But if he is also a part owner, the right of a majority of the others to remove him has been questioned. Yet the better opinion is, unless he controls one-half or more of the shares of the vessel, he may be removed from his position of master at the will of the majority, even though no cause for removal be assigned.

46. Generally, a master has nothing to do with the cargo beyond receiving and delivering it. But should necessity require, he may sell it, or a portion at an intermediate port, whenever he cannot carry it farther, or without perishing before he can receive specific orders. Again, he may sell it, or a portion, or pledge

it to raise money, for the common benefit of the owners of the ship and cargo.

47. An owner is liable for the wrong-doings of the master while he is acting in that capacity. But he is not liable for his wrongful acts when not thus acting, although at the time holding the office. Thus, if through want of skill or care, he should run down another vessel, the owner would be liable for the collision; but he would not be liable should the master quarrel with a man and beat him on shore, or even on the deck of his vessel; nor would the owner be liable should the master wrongfully take goods on board his ship to derive a profit from them.

The loss of a vessel, though in charge of a part owner, not caused by his negligence or wilful misconduct, falls on all the owners. But when the loss can be traced to the fault of a part owner, every other owner has a right of action against him for the value of his share.

48. The general rule of liability in this country for collisions is, when both parties are equally in fault the loss is apportioned between them. When neither party is at fault the loss rests where it falls. When the fault is wholly on one side the other can recover full compensation.

49. The execution of shipping articles is required by federal statute where the vessel is bound on a foreign voyage or from a port in one state to a port in any other than an adjoining state; and if this statute is not regarded, the seaman has the right to leave the vessel at any time, and may recover the

highest rate of wages prevailing at the port of shipment.

The articles must be signed by the seaman and by the master, and must be executed before the vessel proceeds on its voyage. Furthermore, with some exceptions, they must be signed in the presence of a shipping commissioner. Nor can they, after signing them, be varied by verbal agreement made by the master and seaman. Statutes providing that all interlineations and erasures in the articles shall be deemed fraudulent, working no change in the papers unless satisfactorily explained, do not apply to immaterial erasures.

To comply with the law, the articles must specify clearly, definitely and precisely, the nature of the intended voyage; the port or country at which it is to terminate, and the duration of the voyage. Indefinite articles, leaving to the option of the master whether the voyage will be long, to one or more foreign ports, or short, to nearby domestic ports, are void.

50. Seamen have a lien on the ship and on the freight for their wages. By an ancient rule freight is said to be the mother of wages, and consequently any accident or misfortune whereby a ship cannot earn its freight money destroys the claim of the sailors for wages.

51. Provisions of due quality and quantity must be furnished by the owner, and double wages are given to seamen who are on short allowance, unless the necessity is occasioned by some peril of the sea or other

accident of the voyage. The master at any time may put them on a fair and proper allowance to prevent a waste of food.

52. Should they doubt the seaworthiness of the vessel, she may be examined at home or abroad on the complaint of the mate and a majority of the seamen. After shipping, if they refuse to embark on the voyage, because the vessel is not in a fit condition, they may be arrested and a court will inquire into her condition, and on finding the complaint of the seamen justified in some degree, will discharge them, otherwise they will be held guilty.

53. The law also requires that every ship shall have a proper medicine chest; and a monthly deduction is made from the wages of seamen to create a fund for maintaining marine hospitals to which they may go without charge.

54. The right of a seaman to be brought back to the home is guarded by law. A master on his arrival at the home port must account for any absence. If he discharged a seaman abroad with his consent he must pay to the American consul three months' wages. Two-thirds of this sum is given by the consul to the seaman, and the other third is remitted to the United States Treasury to form a fund for bringing home seamen. Of course, this obligation does not apply to a voyage that has ended by a wreck or similar misfortune.

55. Persons are employed to repair ships and furnish them with supplies. They are called materialmen. Such persons and all who work about a vessel,

like stevedores, who load and unload, have a lien thereon for their charges. Though by common law material-men have a lien only on foreign ships, in many states by statute they have a lien on all ships, whether domestic or foreign. The lien extends beyond mere repairs to alterations and to rebuilding, but not to the general construction of a vessel. The labourer employed in general work by a shipwright or mechanic has no lien on the vessel for his labour. The liens thus established by statute take precedence of the claims of all other creditors.

One who renders services or furnishes supplies to a vessel and is also a part owner is not thereby deprived of any lien he would have were he not an owner. But he has no priority over other creditors.

56. In general, every part owner is liable for all the repairs of his ship, or for necessaries that are supplied in good faith.

(a) A credit given, or intended to be given to a part owner personally, cannot be charged to others. If goods are charged to a ship, or to a ship and owners, this would tend strongly to show that it was the intention of the person who supplied them to do so on the credit of all the owners. If, on the other hand, they were charged to one owner this would prove that credit was intentionally given to him alone.

(*b*) How far a part owner can bind the others for necessary supplies and repairs is not as well settled as this important question ought to be. Chancellor Kent long ago wrote as the law presumed that the

common possession of a valuable thing would lead all to do whatever was necessary to preserve it, part owners had an implied authority from the absent part owners "to order for the common concern whatever is necessary for the preservation and proper employment of the ship." And this view is sustained by the Supreme Court of a state that has often decided questions relating to the law of shipping. "We think it is true, as a general proposition, that a part owner of a vessel, in undisputed possession, will be regarded as having implied authority to bind the other owners for things necessary for the vessel and its employment, unless the evidence discloses something to indicate that such implication of agency is contrary to the fact. As to one who furnished materials to make the vessel seaworthy, upon the order of a part owner in such possession, even if it be in the home port, the presumption remains, unless there is something more than the single fact of the place of registry or enrollment of the owner's residence, to remove it." [1]

(*c*) Again, the person holding the beneficial title to a share in a vessel is liable as part owner. A person, therefore, who is no longer entitled to profits is no longer liable for repairs. But when a transfer of ownership occurs during a voyage the former owner may be liable for repairs pertaining to the ship during that voyage, and also the profits accruing therefrom, unless the transfer provides otherwise. Even then it may be quite beyond the possibility of the parties

[1] Bowen v. Peters, 71 Me., 463.

to change the former's liability to a third person who has contracted or furnished materials by reason of such ownership.

(*d*) As a general rule one part owner may bind others for necessary supplies and repairs for a ship procured on credit. This authority may be modified, controlled or negatived by other things. Thus if he has actually parted with his interest, though is still a registered owner, or has committed the vessel to the exclusive control of the other owners, or has given notice to incur no more expense, and has so informed the ship's husband. In such cases he will not be liable for supplies and repairs unless in some way he has misled the furnishing party.

57. A tonnage tax is demanded on the entry of a vessel coming into a port to trade. It is levied only on foreign vessels, or vessels coming from some foreign port or place. A duty of fifty cents a ton, denominated "light money," is levied and collected on all vessels not of the United States which may enter our ports. Such light money is levied and collected in the same manner and under the same regulations as tonnage duties. The collector may refuse to enter or clear a vessel which has not paid her tonnage duties, and if he neglects to do so, the United States has an action against the owner, and also the ships, but not against the consignee of the vessel.

58. It is a criminal offence for any person not in the United States service and not authorised by law to go on board of a vessel about to arrive at her

port of destination before her actual arrival without the master's permission, regardless of his motive and the subsequent permission of the master to remain on board.

CHAPTER XX

MARINE INSURANCE

1. Nature of the contract.
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6. Policy may be transferred.
7. But insurer must consent.
8. Insured must be interested in the property.
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17. So can freight money.
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23. Other implied warranties.
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34. Perils enumerated:
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42. How a general average usually arises.

1. The contract of an insurance binds the insurer to indemnify, or make good the insured against loss or

injury to the ship, or his interests therein, from specified perils. The consideration for the contract on the part of the insurer is the premium paid to the insured. The contract of insurance is called a policy. No instrument is needful to make such a contract valid; if the proposals of the insured are written in a proposal-book and signed by a proper official with the word "done," or "accepted," or in any way that indicates a bargain, they are valid even without a policy. Indeed, it has been asserted that an oral contract of insurance would be legal.

2. The form of policy in general use is familiar both to the insurer and insured, for it has been in existence many years, both in England and in this country. Of course, changes have been made, but its general features have long been known.

3. It is signed only by the insurer, though binding both parties. It may be made on the application of an agent of the insured whenever he has proper authority for this purpose.

4. A party may be insured who is not named by using the words, "for whom it may concern," or others of a similar character. A person who seeks to have the benefit of such a policy must show that he had an interest in the ship at the time of insuring her. Another phrase is, "on account of owners at the time of loss." This will cover all the losses of all persons for whom the policy was intended, who then owned the ship, though there may have been transfers between the time of insuring and her injury or destruction.

5. Alterations may be made at any time by consent, but a material alteration by the insured without the consent of the insurer discharges the latter, though made honestly, believing or expecting that he would readily consent. A material mistake of fact in the policy can be corrected by legal proceedings if the parties themselves cannot agree to a proper amendment.

6. A policy may be transferred or assigned, and the assignee may sue, should occasion require, in the name of the assignor. An insurer's assent to the transfer does not always make a contract between him and the assignee in which he can sue in his own name. A loss made payable to order or to bearer is negotiable by indorsement or delivery, but the transferee cannot even then sue in his own name. When the insured transfers the ship with the consent of the insurer, without transferring the policy, the policy is discharged or ended, unless it was expressly made for the benefit of whoever should be the owner at the time of loss.

7. There is usually a clause to the effect that the policy is void if assigned without the insurer's consent; but this does not apply to a transfer effected by law; for example, insolvency or death. And after a loss has happened the claim against the insurer may be assigned.

8. The contract of insurance is one of indemnity for loss. The insured must therefore be interested in the ship at the time the loss happened. A mere possibility or expectation cannot be insured, but an actual interest in a vessel may be. The owner or goods may

insure them, and can recover for their value when they are lost. Also, one who has taken a risk, or agreed to indemnify another, may insure himself against the risk. Again, the lien of one who repairs a house or ship is an insurable interest. And generally any person who has possession of a ship, house or merchandise, or a right to the possession, like a factor, consignee or carrier, may insure his interest. But indebtedness to a creditor for money borrowed that may have been used in buying a ship does not give him the right to insure her.

9. The value or sum to be paid in the event of loss may be fixed by agreement in the beginning and stated in the policy. It is then called a valued policy. Or, the agreement may be that the amount shall be ascertained by proper evidence, and the policy is then called an open policy.

10. This valuation, made in good faith, is binding on both parties, even though it be very high. But a wager policy—in other words, one not founded on value—is void.

11. One thing insured may be valued and not another; or the same thing may be valued in one policy and not in another. If only a part of the goods included in the valuation are on board, it applies to them proportionately. A valuation of an outward cargo will generally be taken as a valuation of a return cargo substituted for the other by purchase, and is covered by the same policy.

12. A valuation of freight applies to the whole cargo; and if a part only is risked it applies in proportion. If

profits are insured they are generally valued. Very often they are insured by valuing goods high enough to include all the profits.

13. In a policy there is usually added to the description of the ship, "lost or not lost." By this phrase the policy operates in the past, and is effective, even though the ship be not in existence at the time of insuring her.

14. The description must identify the thing insured by quantity, marks, numbers, size, or in some other satisfactory manner. The phrase, "a return cargo," will generally apply to a homeward cargo of the party insured in the same ship, but the word "proceeds" or "returns" is generally regarded as limited to a return cargo, bought by means of the outward one.

15. It is common to cover the freight by an overvaluation of the ship, but an open policy on the ship does not cover the freight. An owner of both ship and cargo may cover by the word freight what his ship would earn by carrying a cargo for another. Insurance on freight from one port to another covers the freight on goods taken by agreement at intermediate ports.

16. A cargo which is lawful may be insured and this may be done, even though it was purchased with the proceeds of an illegal voyage.

17. Freight money,[1] or money that is to be paid for carrying goods, is often insured. An interest in freight

[1] In insurance the term includes the money to be paid to the owner of the ship by the shipper of the goods, and the earnings of an owner by carrying his own goods, for their value is increased by carrying them from one place to another; also the amount to be paid to him by the hirer of his ship and the profits of the hirer either by carrying his own goods, or by carrying for pay the goods of others.

money begins as soon as the ship is actually ready for sea, and goods are put on board, or are ready to be thus placed, or are promised to be put on board by a contract that is binding on their owner.

18. Marine policies generally provide that the insurer shall be liable only for that part of the ship or other thing insured not covered by prior insurance. The second policy covers what the first leaves, the third what is left by the second, and so on. Whenever the whole value of the ship is covered by three policies, for example, later ones are of no account. In no event can more than the loss or indemnity be recovered. If all of them take effect at the same time, and afterward the property diminishes in value, then all of them are diminished.

19. A stipulation in a policy that a certain thing shall be, or shall not be, is a warranty; and there must be an exact compliance with it. The excuse is not good that the thing is not material, or not known, or that it was caused by an agent of the insured.[1]

20. The usual subjects of warranty are: first, the ownership of the property, which is chiefly important because it secures neutrality or freedom from war risks of the property insured. Again, the neutrality of the ship is sometimes expressly warranted, which is not broken if part of the cargo that is not insured belongs to an enemy. The neutrality of the ship or the cargo must be proved by having on board all the usual and regular documents.

21. Second, is the time of the sailing of the ship.

[1] A warranty is legal though written on a separate paper, to which the policy refers.

She sails when she weighs anchor or casts off her fastenings and gets under way, even though she stops afterward and is driven back. Even though ready and intending to go, but stops before getting under way, is not a sailing.

22. Besides express warranties, others are implied. (*a*) One of them is seaworthiness. By this is meant that the ship in every respect is able to begin and prosecute the voyage proposed, and encounter safely the common dangers of the sea.

(*b*) There cannot possibly be a definite and universal standard for seaworthiness. A coasting schooner must have one kind of fitness, a freighting ship to Europe another. The same remark applies to the crew, pilot, furniture, also the rigging or sails. In all these respects much depends on usage. Parsons says there is no better test than this: "A ship must have all of these things in such quantity and of such quality as the law requires, providing there is any positive rule of law affecting them; and otherwise such as would be deemed requisite according to the common consent and usage of persons engaged in that trade."

(*c*) As a policy is binding on a seaworthy ship, no violation of it afterward by the insured discharges the insurer from liability for a loss that happened before its violation. Again, even if a policy is not binding at the beginning of the voyage, by quickly remedying the unseaworthiness, the policy binds both parties.

(*d*) When unseaworthy the master must repair her at sea if this be practicable, either with his own means or with the aid of another ship; when this cannot be

done he should not keep her at sea if he can readily make a port where she can be made seaworthy. Having entered, his ship should not leave so long as she is in an unseaworthy condition provided she can be made seaworthy there. If leaving sooner, the insurer is no longer liable; but the liability may not be destroyed, but only suspended, if she is made seaworthy at the next port.

23. There are other implied warranties besides seaworthiness. One of them is that the insured shall deal honestly with the insurer, and make a distinct and true statement of all the circumstances affecting the risk. Another is that the ship shall pursue the usual course of her voyage and without deviation.

24. There must be no misrepresentation concerning the character of the ship. Nothing should be concealed, for misrepresentation or concealment discharges the insurer. Many questions have arisen concerning the nature of the representation. Any statement in reply to a distinct inquiry will be deemed material. On the other hand, the insured is not bound to communicate any mere expectation, or hope, or fear, but only facts material to the risk.

25. Much has been said concerning what things should be made known. Not only should facts be stated by the insured, but also intelligence and rumours, if such matters are important to the risk, and it has been asserted that intelligence known by the clerks of the insured is presumed to have been known by him. If the voyage proposed should violate a foreign law not generally known this should be mentioned. Indeed,

everything should be included that might reasonably be considered in estimating the risk. Obviously the season, or political events, or the character of the voyage may make a thing material in a particular venture that would not be in other cases.

26. The insured need not state to the insurer things he already knows, or may be supposed to know; matters are as open to the insured as they are to the insurer. For example, general facts widely published and generally known by all who are interested in shipping. Likewise, things resting on a general rumour known to all alike—facts of science, the position of a port, the peculiar dangers or liabilities of any well-known navigation; the course of winds, currents or weather.

27. Should either party say something to the other that ought to put him on inquiry and none is made, he must bear the consequences.

28. A false statement concerning the terms on which other insurers have taken the risk will vitiate a policy. And so will a statement that an old ship is new, for her age is an important fact in determining the premium that ought to be demanded. Again, if different policies are on the same vessel and relate to each other, a false statement or misrepresentation to the first insurer is regarded as passing onward and affecting every other.

29. Every statement or representation should be construed fairly so as to include all just and reasonable inferences. A substantial compliance will suffice.

30. The premium is due when the contract of in-

surance is completed, but in this country the premium is usually paid by a note given on the delivery of the policy, or soon afterward. If the receipt of the premium is acknowledged in the policy this will not prevent an action to get it whenever it has not been paid.

31. Even though the premium is paid, it is not earned unless the risk is incurred, which it not whenever the ship does not sail or had not the goods insured on board. Furthermore, if the premium is not earned in part or in whole, it must be returned, either in whole or in part. But the premium may be partly earned, and then only a part need be returned.

32. Next may be considered the perils covered by policy. An insurer is liable only for extraordinary risks. The very meaning of seaworthiness is that the ship is able to encounter all ordinary perils. If she is lost or injured by an ordinary peril—common weather, for example—the insurer is not liable, because this the ship should be able to withstand. Nor is an insurer liable for loss or injury by wear and tear, or natural decay, or the effect of age, or hard service. Every part of the ship must, of course, decay, and when she is known to be lost the insurer is not liable without sufficient evidence of an adequate cause. Without this evidence the presumption would be that she was lost by reason of her defectiveness, caused by age and natural wear and tear.

33. By perils are meant those incident to navigation, especially those arising from the wind and weather, the rocks, coast, and the like. But it must be remembered that an insurer does not include every-

thing, only those that are extraordinary. Consequently destruction by worms is not such a peril as renders an insurer liable, because it is not extraordinary. They exist in all waters, and at certain seasons the dangers from this cause are very great. Nor is an insurer liable for an injury caused by rats, for, like worms, they are active and dangerous creatures.

For the same reason an insurer is not liable for the loss of any article whenever it was caused by inherent qualities, unless these became destructive by an insured peril. Thus, hemp rots from fermentation, yet it will not ferment when kept dry, consequently insurers are not liable for a loss arising from dampness at the time of taking hemp on board; but if the vessel were afterward strained by tempest and her seams were opened, wetting the hemp, which afterward rotted, the insurers would be liable.

34. Some of the perils may be briefly mentioned. (*a*) One is collision. (*b*) Fire is another, but it must be caused by something extraordinary to render the insurers liable. An insurer would also be liable for any direct and immediate consequences of the fire, and for losses caused by the endeavour to extinguish it.

Perhaps the most general rule is that insurers are liable for the loss or injury that is the natural, direct and proximate effect of an insured peril, although the loss might be the immediate effect of a preceding loss. For example, should a part of the cargo be burned, and another part be injured by water used to stop the fire.

(*c*) There are other perils, like piracy, robbery and theft, that need not be described. There is another peril called barratry, which means the wrongful act of the master, officers or crew, against the owner. As the master is appointed by the owner and is controlled by him, many policies provide that they will not insure against barratry, if the insured is the owner of the ship. The purpose of this is obvious. It is to prevent an insurance of the owner against the acts of one who should, or ought to hold himself responsible. As a general rule, insurers are liable for the misconduct of the crew when all reasonable precautions have been taken by the owner and the master to prevent such misconduct.

35. An owner does not insure any man against his own acts. For the negligence or wilful misconduct of the master or crew the insurers may be liable, because in this respect they are not the agents of the owner. They would indeed be his agents if he directed the wrongful act or negligence that destroyed the property, and in such a case the insurers would be discharged, but we can hardly imagine such a state of things. An owner does not give directions to his servant to be neglectful or to act wrongfully. Consequently, the law assumes that an agent, while wandering from the path of duty, is acting solely on his own account, and not in a representative character.

36. If the cargo is damaged through the fault of the master or crew the shipper has a remedy against the owner of the ship, but this does not discharge the insurers. If, however, the shipper enforces his claim

against them he is bound to transfer to them his claim against the ship-owner. For the insurers of the cargo, by paying a loss thereon, put themselves in the position of the shipper and acquire his rights.

37. Generally no loss will be attributed to the negligence or fault of a master or crew that can be attributed to any of the perils mentioned in the policy.

38. A loss may be total. This happens when the whole property passes away; for example, by sinking or destruction by fire. The law also regards a loss as total when the ship or goods are partly destroyed, and permits the insured to abandon whatever is saved to the insurers, and to claim from them the total amount specified in the policy. The abandonment transfers all that remains of the property to the insurers. If nothing remains, or it possesses no value, there need be no abandonment and yet the loss is total.

39. If the goods of several owners are in peril, and those of one of them are wholly or partly sacrificed for the purpose of saving the remainder, all must contribute toward indemnifying the loser. He is not to be fully indemnified, for then he would be better off than the others, and justice is perfectly satisfied if in the end he suffers like them. This end is attained by a general average. The loss is ascertained and such an assessment is made on the property saved for the benefit of the owners of the property lost as will equalise the loss among all. In this way everyone interested loses an equal proportion of whatever was sacrificed for the common good.

40. The essentials of a general average loss are: First, a common peril impending at the time; second, a voluntary loss or sacrifice of some property for the purpose of saving other property; third, the success of the endeavour.

41. There must be a common peril, for if there be none the loss is merely wasteful. The loss must also be voluntary. There can be no voluntary sacrifice creating a claim for contribution whenever the property destroyed was not merely in danger, but was certain of destruction, because there is no voluntary sacrifice in casting away property that must be inevitably lost. But when the loss of the whole is inevitable, and a part can be saved by destroying the remainder, this is a general average loss for which a contribution should be made.

42. The most common way in which general average arises is by jettison, or the casting overboard of some part of the cargo to save the remainder. If the goods jettisoned are recovered the loss is then only the expense of recovery and restoration, which must be averaged and paid in such a manner as to fall on all in equal relative proportions.

CHAPTER XXI

FIRE INSURANCE

1. Nature of fire insurance.
2. It is now effected by companies.
3. Methods of fire insurance companies.
4. Execution of a fire policy.
5. Rules for construing.
6. Differences between mutual and stock companies.
7. Application for a policy.
8. What is included in a fire insurance policy.
9. Printed conditions.
10. Alterations.
11. An alteration increasing the risk in violation of the contract.
12. Repairs.
13. Interest the insured must have.
14. Trustee's agent or consignee may insure.
15. Insurers must know whom they insure.
16. Warranty and representation.
17. Statements on a separate paper.
18. Use of the word warranty.
19. How statements may be regarded.
20. How a representation differs from a warranty.
21. Concealment.
22. Property must be in existence.

23. Negligence.
24. What proportion a mutual company can insure.
25. What value the insurers of goods must pay.
26. Policies can be assigned.
27. Certificate of loss.
28. Insurers do not pay for losses of profits.

1. Fire is one of the perils covered by marine policies. It is usual, though, to insure buildings and their contents against fire alone. The general purposes and principles of this kind of insurance are the same as those already mentioned, and the law differs only in those ways wherein a difference is necessary by reason of the character of the property insured. This kind of insurance is to indemnify against loss by the burning of ships in port, more often of warehouses and of property stored in them, and still more frequently of goods in stores or factories, or in dwelling-houses or in barns. The most common application of all is to dwelling-houses.

2. Like marine insurance, fire insurance in this country at the present time is effected almost wholly by companies. They are either companies in which persons who own the stock take all the profits as dividends; or mutual companies in which everyone who is insured becomes a member, and the net profits are divided in such a manner as the charter or by-laws of the company may direct. In some cases both forms are united in a single company. In these companies there is a capital stock as a permanent guaranty fund above the premiums received; and a part

of the net profits is paid as a dividend on this fund, while the residue is divided among the insured.

3. The methods of fire insurance companies are quite uniform throughout the country, and any company may appeal to the usage of other companies for answers to various questions. In the first place, there may be an appeal to explain whatever needs explanation, but never to contradict whatever is clearly expressed in the contract. No usage can be admitted even to explain a contract unless the usage is so well established, or so well known, that it may be supposed the parties contracted with reference thereto. And not only must the terms of the contract be duly regarded, but also those of the charter. Thus, if it should provide that all policies and other instruments made and signed by the president, or other officers of the company, shall bind the company, an agreement to cancel a policy should be signed in the same manner.

4. In regard to the execution of a fire policy, there is no material difference between the law concerning fire and marine insurance. An adoption or ratification of fire or marine policy is the same thing as the making originally of the contract.

5. The rules of construction are generally the same in fire as in marine policies. A policy is sufficient if the words describe the persons, the location and the property sufficiently for the court and jury to determine their identity. In construing this, as well as other contracts, the intention of the parties is the most important guide. The intention, however, must

be that expressed in the contract. Otherwise, a contract that was not made would be substituted for the written one.

To this rule there are some exceptions. Thus, clear and positive evidence of the truth may be shown that a written contract does not express the actual and certain agreement of the parties, by reason of an accidental mistake or omission of words.

6. There is one important difference between the contracts of mutual and stock companies. Every person insured in a mutual company becomes a member. Indeed, the principle on which this insurance rests is that all insure each other. Every person insured, therefore, is bound by all the laws and rules of the company as if they were of his own making. And this is equally true of marine and fire policies.

The mutual fire insurance companies require that an application be made in writing after a peculiar form prescribed by their rules. In each form of application various questions are put, suggested by experience, and are best calculated to elicit all the information needed by insurers for the purpose of estimating accurately the nature of the risk they undertake. To this application, with all the questions and answers, reference is made in the policy, and it becomes a part of the contract.

7. Sometimes there is no application in writing, but the policy itself states the facts relating to the risk. For this purpose it contains many blanks that are filled as each case requires. Should these insertions be inconsistent with what is printed they must

prevail, as they are supposed to express the precise purpose of the parties better than the printed phrases that were prepared without special reference to that particular insurance.

8. It is usual in fire insurance to put in the policy a scale of premiums calculated on different classes of buildings, of stock in trade, or other property in conformity with what is thought to be the greater or less risk of fire in each case. This is regarded as a matter of special importance, and if a statement were made by an applicant which put his building or property into a class on which the risk and premium were less than on the class to which the building or property actually belonged, and in that way an insurance was effected at a less premium, the policy would be void, although the erroneous statement was made innocently.

9. If the printed conditions represent one class of buildings, or companies, or properties as more hazardous than another, the insured cannot prove by other testimony that it was so in fact. Besides, the agreement requires that the property insured shall continue within the class where it is put, or at least that it shall not be entered in another that is more hazardous during the continuance of the policy. A liberal construction, however, has been given to this rule. Thus, it does not apply to a single article, or one or two, kept in a store as a part of the stock of goods, although that article—cotton in bales, for example—is among those specified as hazardous. But if the building is appropriated to a more hazardous occupation than the proposals of the policy indicate, or if the introduction

of these goods materially increase the actual risk, evidence may be received of the intention of the parties to the contract. Thus, on one occasion the storing of wine was prohibited as hazardous, yet it was held that having a pipe or two in the cellar, from which similar vessels in the store were replenished, did not come within the meaning of the word "storing" in the policy, any more than would the keeping of such articles for home consumption in a dwelling-house insured by a similar policy. And if the premises are described as a private residence the insurance is not rendered void by the fact that the occupants moved from the house, leaving it vacant, unless the risk was thereby materially increased.

10. The subject of alteration of property insured is somewhat difficult. Mere alterations, though they may be expensive and important, do not necessarily avoid the insurance, or discharge the insurers. But whenever they have the effect of increasing the risk, or are prohibited in the policy, they become invalid.

Suppose one gets his dwelling-house insured for seven years and describes it correctly as having a shingled roof, but after two or three years the shingles are taken off and slates are used. The risk is not increased nor is the risk of putting on the new covering hazardous, and doubtless in such a case the policy would not be avoided. Suppose a metallic covering is put on that requires soldering; this, surely, is a hazardous operation, and if the building should take fire while making the change the insurance would be discharged. But after safely finishing the operation

there would be no greater hazard from the use of such a roof than from the old one. Again, suppose that while the operation was going on the house was exposed to a greater risk from the outside, and was set on fire by an incendiary, would not the insurer be discharged?

11. An alteration which is permanent and causes a material increase of the dangers of fire is a violation of the contract and discharges the insurers. Not only so, but as soon as the preparations for it are begun—for example, the erection of scaffolding to do the work, or any other preparation materially affecting the risk—the insurers are discharged.

12. The insured has a right to keep his building in good repair; indeed, it is his duty, as well as the interest of the insurer that he should do so, for any condition of disrepair would tend more or less strongly to increase the risk of fire. The insured, therefore, may repair without obtaining leave to do so, and the insurer is always liable, although the fire takes place while the repairs are in progress. It may be added that the fire policies most frequently in use give the insured the right of keeping the property in repair.

13. With respect to the sufficiency of the interest of the insured to support an insurance, the same principle applies as in marine insurance. A legal interest is sufficient. One who has made only an oral bargain with another to purchase his house cannot insure it; but if he made a written contract the purchaser may insure. Again, a debtor, who assigns his property to pay his debts, has an insurable interest therein un-

less the property is sold. A mortgagor also may insure the whole value of his property, even after transfer of possession to the mortgagee, provided his right to recover the same is not wholly gone. Again, both a mortgagor and a mortgagee may insure the same property, and only one of them need specify his interest.

14. A trustee's agent or consignee may insure against fire, as he may against a marine loss. Generally a consignee is not bound to insure against fire, but may do so at his discretion. The agent of goods held on commission may insure expressly his own interest in them for advances, or he may insure only the owner's interest. When the interest is not expressed the policy will be regarded as not covering the interest of the owners if, on a fair construction of the words and facts, it seems to have been the intention of the party to secure only the consignee's interest. It is now a common thing for a commission merchant to cover in one policy in his own name all the goods of the various owners that have been consigned to him. "Goods held on commission" in fire policies have the same effect as the words, "for whom it may concern" in marine policies. A consignee of goods may insure his own interest in them against marine or fire risks. So, any bailee, or person in possession of goods, although for a short time, may insure them against the fire. Thus, a common carrier by land, who has a lien on goods and is answerable for their loss by fire, may insure them for their full value.

15. Insurers must know the insured. Not infre-

quently companies decline to insure persons, because they are so neglectful in caring for their property, and perhaps are suspected of destroying it wilfully.

16. The law of warranty and representation is the same in fire as in marine insurance. A warranty is a part of the contract and must be distinctly expressed and written either on the policy, or on a paper attached to the same, forming an essential part. The warranty may be of a present or future character. The warranty may also be a continuing one, rendering the policy void by the non-continuing of the thing that is warranted to exist. Whether it is continuing or not must evidently be determined by the nature of the thing warranted. A warranty that the roof of a house is slate, or that there are only so many fireplaces, or stoves, would generally be regarded as continuing; but a warranty that a building was five hundred feet from any other would not render the policy invalid if a neighbour should erect a house within one hundred feet without any knowledge of the insured.

17. Statements may be made on a separate paper; in such cases it is usual to refer to them in the policy in such a manner that both shall form one instrument.

18. The word warranty need not be used if the language clearly imports, or means the same thing, and an indorsement on a policy before its execution may take effect as a part of it.

19. In a policy may be made a statement which is not to be regarded as a warranty by the insured, but

merely as a license or permission of the insurers that the premises may be kept in a certain way; for example, the statement that a dwelling-house "is to be hereafter occupied as a tavern."

20. A representation differs from a warranty in this respect, that it is not a part of the contract. Of course, when made after the signing of the policy, or the completion of the contract for insurance, the contract is not affected. When made before the contract and for the purpose of effecting insurance, a false and material representation, though forming no part of the contract, avoids the policy. The true answer to a question of this kind is whether or not the contract would have been made, and in the same terms if the statement had not been made to the insurers. If the answer is that they would have declined to make such a contract, then the statement is material, otherwise it is not.

21. Concealment is the opposite of representation. The insured is bound to state all that he knows himself, and all that the insurer ought to know for the purpose of estimating correctly the risk assumed. A suppression of the truth has the same effect as expressing what is false. Insurers must be understood as knowing all those matters of common information that are as much within their reach as that of the insured; these therefore need not be especially stated. But special circumstances, for example, that many fires had taken place in the neighbourhood, and the probability or belief that incendiaries were at work, should be made known; and any questions asked must

be answered as fully and precisely as they require. Concealment in an answer to a specific question can rarely be justified by showing that it was not material.

22. At the time of insuring the property must be in existence and not on fire, nor exposed to a dangerous fire in the immediate neighbourhood, because the insurer assumes that no unusual risk exists at that time. Insurers are not liable if the property be destroyed or injured by the indirect effect of excessive heating, or by any effect which stops short of fire or combustion. But if there be an actual ignition, or lighting, they are liable for the immediate consequence; for example, for the injury from water used to extinguish a fire. In some instances policies require that the insured shall use all possible diligence to preserve his goods; such a clause would strengthen his claim for insurance, should they be destroyed after making an effort to save them by removal. So the insurers are liable for the injury or loss sustained by the blowing up of buildings to arrest the progress of fire. As lightning is not fire, if property be destroyed thereby, the insurers are not liable unless there was ignition. An explosion caused by gunpowder is a loss by fire, but not an explosion caused by steam. In science it might be difficult to distinguish between these two causes, but the law makes distinctions of its own.

23. Whether, when the negligence of the insured or his servant is regarded as the sole or direct cause of the fire or loss, the insurers can be held, has been already considered. A loss caused by the negligence

of the insured himself, so extreme and gross as to strongly indicate the conclusion that he was guilty of fraud, would be an effective defense. A fire caused by the insanity of the insured would be no defense.

24. Mutual companies are usually forbidden by their charters to insure more than a certain proportion of the value of a building. Of course, the insured can never be held to pay more than the sum mentioned in the policy. But the charter or by-laws permits a company to insure only a certain proportion of the value, three-fourths, for example, and if more than that sum is insured, it is not required to pay more than the three-fourths; and the person insured cannot show that the building was really worth more than the additional one-fourth. On the other hand, the valuation, if honestly made, is binding on the insurer and he cannot prove that the building is worth less. Sometimes a policy reserves to the insurers the right to have a new valuation made in the event of loss. In such a case, if a lower valuation is made, the insurers are required to pay only the same proportion of the new valuation which they had insured of the former valuation.

25. The sum that insurers of goods must pay is their value at the time of the loss; and a fair sale at auction is generally taken as a correct valuation, provided the insurers had reasonable notice or knowledge that the auction was to take place.

26. Policies against fire are personal contracts and do not pass to any other party without the consent of the insurers. Of course, assignments are made

with the consent of the insured. In all cases the rules or usages of the insurers in this respect must be regarded.

27. When a policy requires a certificate of the loss this must be presented to obtain the insurance money. If the policy requires notice to be given forthwith there must be no unreasonable or unnecessary delay. In fire policies, as the premises are supposed to be always open to the inspection of the agents of the insurers, a general notice of fire will probably suffice. Of course, the insurers may waive their right of notice wholly or partly, and they may do this expressly, or by any acts fairly indicating to the insured that they accept an imperfect notice given to them, or that they have taken the matter into their own hands and have made inquiries and obtained all the information desired. And a refusal to settle the claim in any way has been regarded as a good excuse for not giving a notice.

28. Insurers against fire are not held to pay for losses of profits gains of business or other remote consequences. Most of the fire policies used in this country give the insurers the right to rebuild or repair premises injured by fire instead of paying the amount of the loss. If, under this power, insurers rebuild a house, for example, that has been insured, at less cost than the amount specified in the policy, they are nevertheless the insurers of the new building for the difference between the cost and the amount they had insured during the unexpired period covered by the policy. And if repairs are made by the insurers

they must be begun within a reasonable time, which is a question of fact to be determined in the same manner as every other whenever the parties are unable to answer it themselves.

CHAPTER XXII

LIFE AND ACCIDENT INSURANCE

1. How life insurance is effected.
2. How the premium is paid.
3. Who are the beneficiaries:
   - *a.*—What children,
   - *b.*—What relation,
   - *c.*—When insurance may be paid to widow of insured,
   - *d.*—When policy is payable to legal representatives, who are meant,
   - *e*—Policy payable to an estate,
   - *f.*—Policy payable to wife and children.
4. Beneficiary has a fixed or vested interest in the policy.
5. Rule does not apply to certificates issued by mutual benefit associations.
6. Beneficiary may pledge his interest.
7. Insured may reserve the right to change the beneficiary.
8. Payment of the premium.
9. Waiver of payment.
10. Forfeiture of policy.
11. Beneficiary must have an interest in the life insured.

12. When execution and delivery of policy are not essential to complete the contract.
13. Policy may be assigned.
14. Notice of assignment must be given to the company.
15. Assignment by holder of policy as collateral security.
16. Warranty, representation and concealment.
17. Good faith must always be observed.
18. Statements concerning occupation.
19. Habits. Use of liquors.
20. Narcotics.
21. Meaning of good health.
22. Dangerous diseases.
23. Physical injuries.
24. Consultations with doctor.
25. Family history.
26. Suicide.
27. Death by operation of justice.
28. Importance of time of death.
29. Effect of other insurance.
30. What is accident insurance.
31. What accidents are included.
32. Are often issued to travellers. What accidents are included.
33. Insurance against poisonous substances.
34. What occupations are included.
35. Occasional act is not another occupation.
36. Liability for injuries causing no external signs.
37. Liability for voluntary exposure.

38. Meaning of phrase "voluntary exposure to unnecessary danger."
39. Meaning of "bodily infirmity or disease."
40. Accidents intentionally inflicted.
41. Death from unlawful act.
42. Injury resulting from intoxication.
43. Employer's insurance.
44. Payment of premium by employer for employee.
45. Policy is broadly construed.
46. Indemnifying for injuries to non-employees.
47. Fidelity insurance.

1. LIFE insurance is usually effected in this country in the same manner as fire insurance, by insurance companies. An application is made by the insured, containing numerous questions that are asked by the insurers relating to the probability of life. These must be answered fully. In some cases questions also are to be answered by the physician of the person insured, others by his friends or relatives.

2. The premium for insuring for a year only, or less, is usually paid in money or by a note. For a period of more than a year the premium in most cases is payable annually. Sometimes a part of the premium is paid in money and a part in notes, which, however, are rarely paid unless the amount is needed to pay losses.

3. The insurance belongs to the person who is designated as the beneficiary in the policy. But it is sometimes difficult to determine who is the beneficiary.

(*a*) For example, if the policy on the life of a mar-

ried man be payable to the children of the insured, who are included? Those by a former wife are, but not the children of his wife by a former husband. Children also includes an adopted child, but not a grandchild. Again, the by-laws of a company requiring the insured to designate as a beneficiary some one dependent on him, means one who is actually dependent on the insured for support. It therefore includes a wife, but not a creditor.

(*b*) By relations are included those by marriage as well as by blood, but not an illegitimate child.

(*c*) A policy payable to the executors, administrators or assigns of the insured, unless settlement shall be made by virtue of an article providing that the company may pay the sum insured to any relative by blood or connection by marriage of the insured, or any other person appearing to the company to be entitled to the same, is authority to pay the policy to the widow of the insured.

(*d*) The phrase "legal representatives" generally refers to the executors or administrators, rather than to the heirs or next of kin of the insured. In a life insurance policy these have a different meaning; they refer to the heirs of the insured, and are sufficiently broad to cover all persons who stand in his place and represent his interests.

(*e*) When a policy is payable to an estate it may be collected by the legal representative of the insured.

(*f*) By the weight of authority a policy payable to a wife and children conveys to the heirs of a child who

dies before the insured the interest of the deceased child.

Likewise the proceeds of a policy—whereby a wife insures her interest in the life of her husband for her own benefit, if she survives him, otherwise for the benefit of his children, and dies during his lifetime leaving children surviving her, who also die during his life—go to the administrator of the children and not to the estate of the insured.

4. Generally, in insuring one's life when no power of disposition is reserved to the insured, the beneficiary acquires in the policy a vested right which cannot be impaired without his consent. In Wisconsin it has been declared that the insured may dispose of the policy by will to the exclusion of the beneficiary, when he has paid the premium and kept control of the policy.

In many states statutes exist which protect the interest of a married woman and her children, as against the claims of creditors of her husband in the proceeds of a life insurance policy on his life.

5. This rule does not apply to certificates issued by mutual benefit associations. By them beneficiaries do not acquire any vested rights. Says the Supreme Court of Indiana, the essential difference between a certificate of membership in a beneficial association and an ordinary life policy is that in the latter the rights of the beneficiary are fixed by the terms of the policy, while in the former they depend on the certificate and rights of the member under the constitution and by-laws of the society. In the one case

the rights of the beneficiary are fixed and vested from the moment the policy takes effect. In the other they are subject to such changes as the law of the associations authorise the society and the member to make.

6. The beneficiary may also dispose of his interest in the policy by pledge, mortgage, or gift.

7. The insured may reserve to himself the right to change the beneficiary at will. This is often done. In such a case the original beneficiary acquires no vested interest in the policy or its proceeds until the death of the insured.

8. As the parties may make any agreement they please about payment of the premium not contrary to statute or public policy, they may agree that the policy shall be forfeited for non-payment of the premium on the appointed day. But a forfeiture is not favoured "and a party who claims a forfeiture must show a fairly clear right to insist upon it."[1] This question most frequently arises when premium notes are given. Such a note executed at the same time as the policy is a part of it. Should the policy provide that if a premium note be not paid at maturity the policy would be void, its non-payment forfeits the policy. But such an agreement must be clearly expressed or it will not be enforced. If the insurer receives money on an over-due premium note from an agent without inquiry, the forfeiture is saved. The premiums must be paid on the days they fall due. When no hour is mentioned the insured has the entire day, even until midnight, to make payment. In some

[1] Ball v. Northwestern Mutual Accident Association, 55 Minn., 414.

policies several days are allowed for the payment of the premium; and an insurer is liable for a loss happening after the premium is due and unpaid, but before its period for payment has expired. Nevertheless, the utmost care is required on the part of the insured to pay his premium before or at maturity. By delivering a policy which on its face acknowledges the receipt of the first premium, an insurance company cannot afterward deny the payment. The legal effect of the policy dates from the time of paying the first premium, and not from the date of the policy itself.

If the company accepts a note for the first annual premium and delivers the policy, this is a payment of the premium, even though the note is never paid. The burden of proof is on the party claiming under the policy to show that the first premium has in fact been paid, or the payment waived.

Payment to an agent is sufficient under a policy providing that if payment is not made into the home office within thirty days after the date of the policy it shall be void and of no effect. The time of mailing a check for the premium of an insurance policy is the time of payment, though it does not reach the company until past due.

Again, the placing of a policy of life insurance in the mail with postage prepaid, so that it would in course reach the insured before he was taken sick, is a delivery of the policy within the meaning of the clause declaring that it shall not be in force until the payment in cash of the first premium and the

delivery of the policy to the applicant during his life and in good health.

9. Although a policy is not endowed with vitality until the premium is paid, payment may be waived or delayed by the company. The taking of a note would certainly be a waiver.

What authority has an agent to waive the terms of paying the premium? If the insured acts in good faith with the agent, relying on the statements made by him within the scope of his apparent authority, the principal will be bound by them. And if there be any limitation on his power, it is the insurer's duty to make this known to the applicant.[1] Therefore, if a general agent contracts to give the insured time for paying the premium and to accept payment in a specified manner, and forthwith delivers to him the policy of insurance, payment of the premium by the insured as agreed after an injury received by him sustains the contract notwithstanding the clause that "this policy shall not take effect unless the premium is paid prior to the offering of any accident under which the clause is made."[2]

The question has been raised more than once concerning the duty of the insured to read the policy. In one of the cases an application was made on December 12th, six days before the date of the policy. The premium was paid and the policy delivered on December 26th, and the agent stated to the insured that the policy would be enforced for thirteen months from the time of paying the first premium. By the terms of

[1] Kerlin v. National Accident Association, 8 Ind App., 628.
[2] Bane v. Travelers' Ins. Co., 85 Ky., 677.

the policy the next premium was payable on December 12th the following year with thirty days' grace, but the insured died on the 18th of January, having paid but one premium. The question was, what did the insured regard as the time within which his policy could run before expiration? The court held that he was not obliged to read the policy, that he had a right to suppose it ran a year from the time of its delivery, in which case it had not expired at the time of his death. The policy, therefore, by this construction, was not forfeited at the time of the death of the insured.

10. Many policies are called non-forfeitable, though so many conditions are attached to them that they doubtless mean much less than the insured imagines. In some states the statutes provide for the issuing of paid-up policies in place of them. Unless required by statute or agreement, the insurer is under no obligation to issue such a policy. When not knowing of the death of the assured, the policy was surrendered for a paid-up policy, the court reinstated the first policy.

11. Everyone for whom a policy is issued must have an interest in the life insured. The general rule is that any substantial pecuniary interest is sufficient, though not strictly legal or definite.

One who lives with a man as his wife, has an insurable interest though not lawfully married to him.

This applies to a sister who is dependent on a brother for support, and also to all cases in which there is a positive and real dependence. An existing

debt also gives the creditor an insurable interest in the life of the debtor.

12. When the terms of the contract have been settled, the execution and delivery of the policy are not essential. The contract is generally regarded as complete on acceptance of the application and the auditing of the premium. And any act on the insurer's part which leads the applicant to take out no other insurance, supposing that his application has been accepted, will bind the insurer. On the other hand, the insurer is not bound until the application is accepted.[1]

13. A life policy may be assigned or transferred. Many policies are made for the purpose of transferring them; in other words, for the purpose of enabling the insured to give this additional security to creditors. It is an important question, what constitutes an assignment. A delivery and deposit of a policy for the purpose of transfer will operate in that manner without a formal written assignment. So will any transaction that gives to a creditor of the insured a right to receive payment from the insurance fund. A delivery of the policy is necessary; consequently if it remains in the possession of the insured, though an assignment is indorsed thereon of which the insurers have notice, the transfer is not completed. But a transfer may be effected by a separate instrument, which is duly executed and delivered, without actually delivering the policy itself. The mode of assigning or transferring policies is gener-

[1] Allen v. Mass. Mutual Accident Association, 167 Mass., 18.

ally regulated by the by-laws of the insuring company or by the terms of the policy.[1]

Under the New York statute, which authorises a married woman to insure her husband's life for her sole use, a policy was held to be not assignable. Said the court: "policies of life insurance in favour of the wife on the life of the husband, we have persistently held to be non-assignable. We have determined that their peculiar character and purpose necessarily took from them their most important characteristic and purpose in general." By a subsequent law such a policy may be assigned with the written consent of the husband.

14. Generally the company requires notice of an assignment; and if this be not given the policy is thereby invalidated. The notice is sometimes held to be directory, and not to affect the legality of the transfer as between the insured and the assignee. Surely no one but the insurer can question the validity of an assignment without notice.

As the intention of the parties must govern the transfer of the policy by delivery with a verbal direction concerning the distribution of the proceeds is a good assignment, even though the policy requires this to be done in writing.

15. The assignee of a policy held as collateral security for a debt of the insured cannot sell or surrender it to the company for its cash value without giving the insured a reasonable time to redeem, but the assignee has a right under ordinary circumstances to

[1] For forms of assignment of policy see Vol. VI, Appendix, No. 12.

assign the policy to another party. Thus, one who holds a policy as collateral security for the payment of a note may assign it to the indorsee of the note and confer on the assignee a right to hold the policy as collateral for the note itself.

16. The principles concerning warranty, representation, and concealment are the same as those already considered relating to fire and marine insurance. In life policies, however, the questions cover more ground, and the answers contain more difficulties, especially in discriminating between what the insured knows and what he believes. If he says simply "yes," or "no," this in most cases is a warranty and avoids a policy when there is a mistake in the reply; but if he answers, "to the best of my knowledge and belief," he warrants only the fact of his belief and nothing more.

Thus, the risk increases with age, but an unintentional mistake of a short period is not material and will not avoid the policy. But an applicant who said he was thirty when in truth, he was thirty-five went too far. On the other hand, an applicant who states his age "to the best of his knowledge and belief," and stipulates that any undue or fraudulent statement shall forfeit his right of recovery, does not thereby forfeit his policy, even though he be three or four years older than his statement unless this was known to be untrue.

17. In every case good faith should be observed. Thus, the policy of a person who, at the time it began to run, was wholly unconscious of his insanity, was

not invalid by the concealment, although two doctors who attended him understood his real condition.

18. A correct answer must be given to a question which requires the applicant to state his occupation. The answer must be substantially correct. But an applicant who states that he is a soda-water maker, when, in fact, he is simply a soda-water seller, is not guilty of a breach of warranty.

Again, an applicant who declared that he was a dry-goods clerk, but failed to state that he occasionally was employed as a bevel smoother of plate glass was not guilty of bad faith.

19. Questions are often asked applicants for insurance concerning their habits, and answers are given that may not be altogether correct. Suppose a question should relate to the use of liquor, an answer declaring one to be of temperate habits does not mean that he is a total abstainer. The Supreme Court of the United States has declared that a man may be of temperate habits, although he once had delirium tremens.

20. In construing a statement concerning the intemperate use of liquors, a court on one occasion said: "An occasional excess in the use of intoxicating liquor does not of itself constitute a habit and make a man intemperate within the meaning of this policy, but if the habit has been formed, and is indulged in to drinking to excess and becoming intoxicated daily and continuously or periodically, with sober intervals of greater or less degree, the person addicted to such

habit cannot be said to be of temperate habits within the meaning of this policy."

Again, an applicant who stated that he never used narcotics was still within the rule of showing that he never used them in such a way as to create a custom or habit.

21. What is the meaning of good health in a life insurance policy? An eminent authority has said an applicant is not required to know and state with absolute certainty his physical condition or his predisposition to different diseases, but it is sufficient that he in good faith discloses fully all that he knows about his past and present health. Sound health means freedom from disease or ailment which affect the general soundness or healthfulness of the system seriously, and the word serious is not generally used to describe a dangerous condition, but rather a grave, important or weighty trouble. A temporary indisposition, such as an ordinary cold, is not an illness within the meaning of that word as used in an application for a policy.

In a well-considered case the Supreme Court of New York said that the word health was a relative term. When one is described as being in good health this does not necessarily or ordinarily mean that he is absolutely free from all and every ill. If the phrase were so interpreted as to require entire exemption from physical ills the number to whom it could be strictly applied would be very inconsiderable.

22. The most important question on applications for life insurance is, whether the applicant is exempt

from any dangerous disease, one which frequently terminates fatally. Some slight physical disturbance, of which in all human probability he will soon be relieved, although it might possibly lead to a fatal disease, is rarely deemed an objection.

23. On one occasion an applicant said: "I have never been physically injured." The court said the reasonable interpretation of the clause was that at that time he was free from serious physical injury and that any injury that he may have suffered from in the course of his previous life had disappeared and left no traces behind that would render him an unfit subject for accident insurance, that he was as to such accidents and their results free from bodily ailments.

24. A false statement concerning a consultation with a doctor invalidates a policy. This rule has been declared, but must have a reasonable construction. The false statement must relate to some substantial injury or ailment, not to a slight or temporary indisposition. Thus, consulting a physician for a cold is not a breach of the condition that the insured has not been under the care of a physician.

25. An insurance company should receive correct answers concerning the family history. It is important to know about disease among its members. Material variation from the truth will render a policy void in this regard. A false answer in response to a question concerning any other insurance will generally invalidate a policy.

26. Once insurance companies had great difficulty in relieving themselves from loss by suicide, though

expressly stating they would not respond for a loss thus caused. The courts drew a distinction between suicide that was voluntary and wrongful, from which the insurer was relieved, and suicide caused by insanity or other disease for which the insurer was responsible. So long as this distinction existed it was difficult for companies to escape payment whenever the insured took his own life. Finally, they adopted a provision declaring they would not pay if the insurer died by his own hand, whether sane or insane. This phrase overcomes all difficulties.

The presumption is always against the fact of suicide, and therefore, while there is a reasonable doubt whether death was due to suicide or accident, the presumption is in favour of the latter. The presumption against suicide is sometimes said to exist only when the insured was insane.

27. It was once a question whether death by order of law discharged an insurer when the policy was silent on the matter. Perhaps the weight of authority is in the affirmative, but the question does not now have much importance.

28. Sometimes the time of death is very important. If a policy be for a definite period the death of the insured must be shown before the end of the period. When nothing has been heard from a person for seven years death is presumed in some states by the common law; in others, by statute. Some companies, however, require absolute proof of the fact of death before paying a policy.

29. The only troublesome question that arises in

reference to other insurance is, whether it includes certificates in a mutual benefit association. On this point the courts divide. In some states such associations are included among insurance companies; in others, excluded.

30. Within a comparatively recent period another kind of insurance has become very general, taking the name of accident or accidental. This includes any actual or unexpected result attending an act. The accident must be the proximate and sole cause of the injury to form the foundation of a recovery.

31. A policy insuring against death or accident caused by external, violent or accidental means, covers death by stumbling and falling against a locomotive engine; a fall due to a temporary and unexpected physical disorder; an accidental strain causing death; a blow struck by another person; to excitement and strain caused by attempting to hold and control a frightened and run-away team; by accidental drowning; by drowning while attempting to rescue the crew of a wrecked ship; a rupture caused by jumping from a train; choking to death while attempting to swallow a piece of beefsteak; injury caused by the sting of an insect; hanging at the hands of a mob; by inhaling gas while working in a well; blood-poisoning; lock-jaw produced by a gunshot accidentally inflicted upon the insured himself; death or injuries caused or resulting from carrying heavy baggage, contact with a poisonous substance, rupture of blood vessel, stooping, death or injuries caused by or resulting from accidental taking of poison, blood-poisoning, discharge of loaded gun,

eating dangerous food, falls, fright, lifting, rupture of tympanum of ear, shooting, strain, suicide while insane, untintentional inhalation of gas. But a rupture caused by jumping from a train, where the insured acted for his own convenience, and not from necessity, was held not to be within the conditions of an accident policy insuring against injury caused by violent or external means. So, sunstroke contracted in the course of the ordinary duties of an architect is a disease, and not an accident caused by external, violent or accidental means.[1]

An insurer may make exceptions. Intentional injuries inflicted on the insured are usually considered "accidental" and come within the proviso that the insurance shall extend to injuries sustained through "external, violent and accidental means." If one dies from disease or bodily infirmity of course this is within the exceptions and the same rule is applied if death is due both to bodily disease and accidents. If death from "inhaling gas" forms an exception, this means by voluntary and intelligent action, and not the unconscious inhalation of gas that is filling a room. Nor is the insurer relieved from liability for death thus caused, by a clause in the policy providing that it shall not cover death resulting from anything accidentally or otherwise taken, administered, absorbed, or inhaled.[2]

32. Such policies are often issued to travellers. The policy covers an accident occurring while the insured

[1] See Bacon on Life Ins., § § 483-490, p. 964.
[2] Menneiley v. Employers Liability Assurance Corporation, 148 N. Y., 596.

is alighting from a train, either at the intermediate station or at his destination. Usually it limits the risk to a conveyance by a common carrier and not to every kind of conveyance. A party who is insured against accidents while travelling by public or private conveyance can recover for an injury sustained while going on foot from a steamboat landing to the railroad station for the purpose of continuing his journey. On the other hand, a person who has left the landing place of a steamer and is injured while walking home cannot recover, because he is not then travelling by a public or private conveyance.

The risks of travel do not extend to an injury sustained in falling from the hay-loft of a livery barn. And if the policy provides that if the injuries "are sustained while riding as a passenger in a passenger conveyance using steam, cable or electricity as the motive power, the amount to be paid shall be double the sum above specified," these words do not apply to one riding on the platform of a railway car.[1]

Again, if the policy require a traveller to comply with all the rules of the carrier while pursuing his journey, he is not thereby bound to inform himself of the carrier's rules, yet he cannot recover, if injured through a known violation of them.[2]

Policies usually contain restrictions or limitations concerning residence or travel; the person insured cannot go beyond specified limits or places without permission. Sometimes the permission is not granted without paying an additional premium.

[1] Ætna Life Ins. Co. v. Vandecar, 96 Fed., 282.
[2] Bon v. Railway Passenger Assurance Co., 56 Iowa, 664.

A policy that prohibits living within a specified degree of latitude, but gives permission to pass as a passenger by the usual mode of conveyance to or from a place in the prohibited limits, is not invalidated by the fact that the insured was compelled by sickness to remain there until he died.[1]

Again, the provision concerning residence is waived by the company's retention of the premium after notice of a breach of the conditions to the agent authorised to receive the premium.

33. Sometimes the policy relieves the company from liability caused by the taking of poisonous substances or the inhaling of gas, introductory to a surgical operation or medical treatment. In such a policy an insurance company is held liable for a death caused by illuminating gas accidentally inhaled while asleep at a hotel. So, too, death caused by the poisonous sting of an insect is not within the exemptions, even though the exemption by poison be expressed in a broad manner—poison in any form or by contact with poisonous substances.

A policy containing this stipulation: "I agree that this instrument shall not be held to extend to poison in any way taken, absorbed or inhaled," relates to the mode or manner of taking poison, and not to the motive of the insured in taking it. The words do not therefore in any way cut off a recovery from the company.

34. The ordinary accident policy insures against accidents arising from occupation or employment. The risks greatly differ; some are so hazardous that com-

[1] Evans v. U. S. Life Insurance Co., 64 N. Y., 304.

panies are unwilling to insure employees against accident. Sometimes the contract provides that if the insured is injured in any occupation more hazardous than that stated by the insurer, the insurance shall only be what the premium would purchase at the rate fixed by the tables for the increased hazard. In such a case the jury must determine whether there has been an increase in the risk or not. Thus, an insured gave his occupation as that of a blacksmith employed by a railroad company; he also acted as a switchman and car coupler. The latter occupation being classed as more hazardous than the former he was allowed to recover the amount the premium paid would have secured in the more hazardous occupation.

The term occupation, refers to the vocation, profession, trade, or calling of the insured. The contract covers all the dangers to his occupation, and he is not precluded from things that are incident to the daily life of men who are occupied, nor from acts of exercise, diversion, or recreation. To enable the insurer to avoid the policy because the death or injury of the insured was incurred in some other occupation than that covered by the policy, it must contain an express provision of this nature. Thus a person insured was a "switchman," the insurer tried to show that when killed he was acting as brakesman. The court declared that his occupation "as switchman did not amount to a covenant that he would do no act not connected with such occupation, or that he would not engage in any different occupation." [1]

[1] Provident Life Ins. Co. v. Fennell, 49 Ill., 181.

35. A mere occasional act, not within the scope of the occupation covered by the policy, is not regarded as engaging in another occupation. Thus, a person who is insured as a grocer may hunt for pleasure, and a person insured as a mining expert does not become an engineer or fireman by riding occasionally on an engine. A banker does not change his employment to that of a sawyer by briefly operating a saw for the purpose of getting some boards wanted for immediate use. But to operate a buzzsaw for one's own amusement is not within the permissible pleasures of a retired gentleman.[1]

36. A provision declaring that there will be no liability for injuries causing no external and visible signs does not apply to injuries resulting in death. Under such a provision the insured is permitted to recover for injuries caused by a strain which produced no external result until some time after the accident. A nosebleed is an external sign of injury.

Whether there are such signs is a question of fact. A discoloration of the shoulder is an external sign, also pallour and grayish look about the face the injury need not be visible to the eye, if it can be ascertained by using the sense of feeling. Again, if the signs of the injury do not appear until some time after the accident, the insured can recover.

37. Accident policies usually exempt the insurer from liability from death or injury caused by voluntary exposure to unnecessary danger or hazard, or perilous adventure. Two classes of accidents are thus excluded

[1] Bacon, § 491, p. 990.

from the risks insured: first, accidents that arise from exposure by the insured to a risk or injury, which is obvious at the time of exposing himself; secondly, accidents that arise from the exposure by the insured to a risk or injury which would be obvious to him at the time if he were paying reasonable attention to what he was doing.

The insured is entitled to recover, even though the accident was caused by his own negligence, unless an exception is made in the policy. This usually provides that the company shall not be liable unless the insured exercises due care for his personal protection. By virtue of this provision he is bound to exercise that degree of care which an ordinary prudent man would use under the same circumstances.

38. The phrase "voluntary exposure to unnecessary danger" has been the subject of much litigation. It means "intentional exposure to a danger; as where a person acts so recklessly and carelessly as to show an utter disregard of known danger, or does an act in the face of a risk and danger so obvious that a prudent man, exercising reasonable foresight, would not have done it. It means dangers recognised, but consciously and intentionally assumed. A policy containing such a provision does not relieve the company from liability for injury which resulted from a voluntary exposure to a danger which was contemplated by the contract. A party who goes out in a boat on a dark night to fish, without a knowledge of the existence of snags which are dangerous to his boat, does not expose himself to unnecessary danger within

the meaning of such provision. Nor does a person voluntarily expose himself to danger by riding in a bicycle race and overexerting himself; nor by cleaning a gun, without the knowledge that it was defective and loaded; nor by visiting a house of ill-fame; and getting shot immediately after leaving the place; nor generally, by doing what a man of ordinary prudence would do under the same circumstances; as by climbing a bank with a loaded gun in his hand while hunting. But there can be no recovery under such a policy for an accident occasioned by jumping from a moving train after it has passed the station; or by attemping to cross through a freight train standing across the highway; or by attempting to lower himself from a window to avoid police officers who were at the door. A person who, with packages in his hands, attempts to cross over a trestle which he knows is dangerous, while there are other ways of travel open to him, voluntarily exposes himself to unnecessary danger. But it cannot be said, as a matter of law, that a person voluntarily exposes himself to unnecessary danger by crossing a railroad trestle bridge where there is a plankwalk and a fence railing on one side. Whether standing on the platform of a moving train which is going at a rapid speed is a voluntary exposure to a known danger, is a question for the jury. Whether under all the circumstances, going on a railroad track or bridge is a voluntary exposure to unnecessary danger, is a question of fact which should be submitted to the jury."[1]

[1] See 2 Bacon, §§ 525, 526.

39. The phrase "bodily infirmity or disease" in an accident policy has been construed on many occasions. In one of the cases the court remarked, concerning the meaning of this phrase: "When speaking of an 'infirmity' we generally mean the state or quality of being infirm, physically or otherwise—debility or weakness; and by the use of the word 'disease' we desire to convey the impression of a morbid condition, resulting from some functional disturbance or failure of physical function which tends to undermine the constitution. We do not, as a general rule, apply either term to a slight and temporary disorder, or to the imperfect working of some function, which is over in a short period of time, and which, when recovered from, leaves the body in its normal condition. In using either of the words we do not, as a rule, refer to a slight and mere temporary disturbance or enfeeblement. If this is true of our ordinary speaking and writing, it is certainly clear that the words should be given no broader meaning when we find them used by an insurance company in a clause of its policy which it relies upon to defeat a recovery thereon." [1]

40. Accident policies insure against accidents intentionally inflicted on the insured by a third person; in many policies this risk is expressly excepted.

Under this clause a court declared that there could be no recovery from injuries caused by fighting, although the insured was not the aggressor. There is

[1] Meyer v. Fidelity & Casualty Co., 96 Iowa, 378.

no liability when one is intentionally shot and killed by another person. This has happened on more than one occasion to a person who has been waylaid and shot by a robber.

41. Another provision bars a recovery when death occurs in consequence of engaging in an "unlawful act." Is this phrase broad enough to cover every unlawful act, whether criminal or civil? The better opinion seems to be that it covers all. Thus, the Supreme Court of Indiana in a recent case has remarked: "A known violation of a positive law, whether the law is a civil or criminal one, avoids the policy if the natural and reasonable consequence of the act does not increase the risk."

Cases have happened of injury to the insured while hunting on Sunday, in violation of the law. In many states the courts have denied a recovery in such cases. In one of them an accident happened while the insured was returning from a hunting expedition. As the statute made both travelling and hunting on Sunday a crime, the insured failed to recover.

42. A contract providing there shall be no recovery for injuries received while the insured is intoxicated relieves the insurer, even though the intoxication was not the immediate cause of the injury.

43. Besides this form of insurance may be mentioned that of employers. The constant risks to which employers are liable from their employees has given rise to this form of insurance. A contract exempting the master from liability from the results of his negligence is void as against public policy; but a contract

with a third person whereby he agrees to indemnify the master is valid.

44. Not infrequently an employee gives an order on his employer for the premium which is to be paid out of his wages. Such an order or assignment covers only the period designated usually, one, two or more months. If therefore it is not paid out of those months, it cannot be paid from the wages earned by him during any others. On the other hand through his failure to pay the instalments on his policy as agreed, the insurer's liability to him is ended. On one of these occasions the court held that the company was not obliged, in order to escape liability, to return to the insured the order and notify him that the contract was at an end, since by its express terms the insurance was to cease at the end of any period if the premium for the succeeding period was not paid.

False representations, which are material relating to his physical or mental condition, or occupation will avoid the policy. The insurer's knowledge of a false representation is a waiver of its effect and actual knowledge by an agent will be deemed the knowledge of the insurer.

45. The employer is insured against loss resulting from his liability for injuries. The law is liberally construed for the purpose of securing to the insured the protection for which he has paid. Thus, a policy insured an ice company against claims for damages on the part of its employees in all operations connected with the business of ice dealers. This language was declared to cover or include only employees in the

operating department. A person, therefore, who was injured while constructing an ice-house was not included in the policy.

A policy was issued restricting injuries to employees engaged in the business of iron and steel works. An employee was injured while engaged in the building department by the fall of a girder. "The general language of the contract," said the court, "is not restricted by any thing in the conditions indorsed on the policy or any way made part of it. If the intention was to restrict such language to operations in any particular department, or to any particular branch of the business or to any particular instrumentality used in said business, it was easy to have said so in unmistakable language."

46. A policy indemnifying for injuries to non-employees resulting from accident caused by horse cars, railways, machinery or appliances used in the business of the insured and described in the application, does not include injuries caused by the use of omnibuses, sleighs, etc., as the risk is different. Whether the risk is increased or diminished depends on the circumstances of the particular case, but the risk in the use of sleighs clearly differs from that in the use of cars.

In recovering for the loss of a member of the body when the policy provides for the payment of an indemnity for the "loss of one entire hand or foot," or the "loss of two entire hands or feet," in order to recover there need not be an actual physical severance of the member form the body. Any loss rendering

the member useless fulfils the agreement. But the loss must be entire if the contract specifies an "entire hand," or an "entire foot." If a policy provides for the payment of a sum for the "complete and irrevocable loss of sight in both eyes," and the insured is a one-eyed man, the insurer is liable if the insured loses the other eye.

47. One other form of insurance may be briefly mentioned—fidelity insurance. This is of still more recent origin. Employers are insured against loss caused by the fraud or dishonesty of their employees. "Guaranty insurance," says Justice Wilkin, "is, in its practical sense, a guaranty or insurance against losses in case the person so guaranteed makes a designated default or be guilty of specified conduct. It is usually against misconduct or dishonesty of an employee or officer, though sometimes against a breach of contract. This branch of insurance is so much more modern in origin and development than fire, marine, life and accident insurance that there are few decisions upon the subject; but the business is gradually increasing and is doubtless destined to take an important place in the commercial world. It may be confidently stated that, notwithstanding the comparative absence of specific decisions, the general principles applicable to other classes of insurance are applicable here as well. Thus, the general doctrine of warranty, representation and concealment, as applied to fire, life and marine insurance, is applicable also to the subject of guaranty insurance." [1]

[1] People v. Rose, 174 Ill., 310.

Fidelity policies usually provide that the insured shall promptly notify the company of any fraud or the mortgagee's title complete, there must be a delivery to do this usually prevents recovery.

CHAPTER XXIII

MORTGAGE OF PERSONAL PROPERTY

1. Once this could not be done.
2. A statutory right.
3. Is not a sale with right to repurchase.
4. A conditional conveyance.
5. How deed must be executed.
6. Property should be described.
7. Future acquired property.
8. Mortgagor may secure contingent indebtedness.
9. Mortgagor need not have absolute title.
10. What statutes require.
11. Recording.
12. What must be done when there is no registration.
13. Mortgagee's right to take possession.
14. Sale by order of court.
15. Mortgagor cannot prejudice mortgagee by making another mortgage.
16. Assignment of mortgage.
17. Maturity of notes of different dates secured by same mortgage.
18. Consequences of mortgagor's neglect to pay instalments.
19. Equity favorably regards mortgagor's retention of his property.

20. Foreclosure.
21. Payment.
22. Mortgage of ship.

1. Formerly a mortgagor could not make a valid mortgage of personal property and retain possession. For, as the common law regarded the possessor of property as the owner his sale of it to anyone in good faith for a valuable consideration, followed by delivery, conveyed a good title to the buyer. While this was the law, the mortgagee had no real security for his loan, consequently mortgages of this character were extremely rare.[1]

2. By statute the mortgaging of personal property has been established probably in every state; and in many respects the mode of making them and the rights of the parties thereto conform to the law of mortgaging real property. The mortgagor is permitted to retain possession until default of payment; indeed, he generally retains possession of his property the same as before.

3. Such a mortgage should be distinguished from a sale with a contract for repurchase. In determining whether it is one thing or the other the intention of the parties is the guide. Often an absolute transfer on its face has been shown to be only a pledge or mortgage.

4. A mortgage of personal property is a conveyance with a condition. It is made to secure a note, either payable on time or on demand. A mortgage may be

[1] For form of mortgage see Vol. VI, Appendix, No. 22.

made for some other purpose, though in most cases it is of this character.

5. In a mortgage of real estate, as we have shown, it is essential to have the writing or deed executed with all the formalities prescribed by law. A chattel mortgage need not be so executed. Indeed, it may be valid even if there be no instrument or writing whatever. This is especially true unless some statute exists requiring more formality in executing the conveyance. Generally statutory forms are prescribed and deeds are made with the same care and recorded in the same manner as mortgages of real estate.

6. The property should be clearly and specifically described so that it can be separated from any other, to be within the protection of the law. A defective description may be cured by a subsequent conveyance. Sometimes a schedule of property is annexed to the deed. This does not enlarge the scope of the mortgage, but is simply what it purports to be, nothing more.

7. With respect to future acquired property the law is still in darkness. In mortgaging property the natural increase therefrom is included or covered by the mortgage; in no other case is future acquired property included unless the deed itself or custom clearly provides for the inclusion. In some cases machinery or stock that is to be added subsequently is covered by the mortgage. Chattels that are to be acquired also pass in the same manner when this is the clear agreement or intention of the parties.

This question often arises in mortgaging goods,

which are undergoing constant change by reason of daily sales and additions. A mortgage that provides for such a change of security is perfectly valid, unless the statute otherwise prescribes.

8. A mortgagor may secure a contingent indebtedness. Indeed, he may secure any payment whatever. Parol evidence may be admitted to show the purposes for which a mortgage was executed, and to identify the note intended to be secured thereby.

A mortgage to secure further advances is valid and any debt that is wholly future may be secured and not merely a present or pre-existing debt. Nor need the amount of intended advance be stated in the mortgage when the purpose is described with reasonable certainty.

To give effect to such a mortgage as against a bona fide purchaser or a judgment creditor, or any other claimant, the mortgagee must show that he has made the advance or incurred the liability mentioned, or that the debt or liability is still outstanding.

Advances, made after the mortgagee has actual notice that others have acquired bona fide rights for value in the property, will be postponed to them, unless it is clearly to the mortgagee's interest that he should make additional advances to protect his interest.

9. It is not necessary that the mortgagor should have an absolute title to property, which is the subject matter of the mortgage. For example, the owner of a chattel not in possession, which is already pledged, may make a valid mortgage of the thing subject to a pre-existing pledge or lien. In such a case notice to

the pledgee or lien claimant would be proper. There may be a prior and junior mortgage of the same thing.

Of course, a mortgage should be a bona fide transaction like any other contract, and be made by competent parties, and based on good morals and public policy.

10. The statutes require the registration of mortgages of personal property. By fulfilling the requirement of a mortgagee usually acquires as perfect title to or interest in the thing mortgaged as that of the mortgagee of real estate. As contests between mortgagees and attaching creditors of a mortgagor are often sharp and bitter, it behooves a person who is taking a mortgage on personal security to have the deed drawn in a careful manner and registered with all the formalities accompanying a mortgage on real estate.

11. The recording or filing of a mortgage is in effect a transfer of the property mortgaged to the mortgagee. If this were not done the attaching creditors of the mortgagor would be justified in taking it unless they had actual notice of the transaction between the two parties. Of course, a mortgage of personal property may be made without recording it or without any writing, which is valid between the intermediate parties, but the object of the writing and registration is to make the transfer effective beyond the parties themselves. By recording an effective notice is given to everybody.

12. When there is no registration, in order to make the mortgagee's title complete, there must be delivery

or change of possession of the property. What this must be depends on circumstances. A mortgagee has been deemed in actual possession from an attaching creditor's point of view by placing a keeper over the mortgaged goods, though concealing somewhat his presence because of the mortgagee's kindly regard for the mortgagor's family. Mortgaged property may in general be delivered and kept by a bona fide agent of the mortgagee. No formal ceremony is essential, but when mere words of delivery are used and the goods remain on the mortgagor's premises, either under his own personal charge or that of his former agent, the change of possession is not sufficient to satisfy the law. Generally, personal property that is mortgaged of which no record is made ought to be taken into the mortgagee's possession to make the title secure against other parties who may make claim thereto as the property of the mortgagor. It need hardly be added that the mortgagee's conduct ought to be honest and open.

13. A mortgage usually provides that if the debt is not paid at maturity the mortgagee may take possession and dispose of the property. The mortgage therefore is a somewhat arbitrary conveyance, as all authority and action relating to the security are confided to the mortgagee.

A law giving to the mortgagee the right to take the property, either absolutely in satisfaction of his debt, or with the right to sell within a fixed time, or at his discretion, and to apply the avails in satisfaction of the debt, and the surplus, if there be any, to the mortgagor, must be faithfully executed. Should the mort-

gagee resort to any trick for selling the property at less than its value, in short, to any way contrary to law, the transaction may be reviewed by a proper tribunal and the wrong perpetrated on the mortgagor may be corrected.

14. The authority to take and sell the property is not always confided wholly in the mortgagee. And if the mortgage be for a large amount it is better for all who are interested therein to apply to the court for an open judicial sale, thereby relieving the mortgagee of all possibility of incurring the displeasure of the mortgagor, or of attaching creditors, or of other parties who may have an interest in the disposition of the mortgaged property. This course is often pursued in disposing of a chattel mortgage and closing the relationship between the two parties.

15. A mortgagor has no right to pledge or mortgage the property of another person or create any other lien thereon prejudicial to the rights of the mortgagee. How far he can sell the mortgaged property is determined by the statute of the state in which it is made, or by the deed itself. If the property is not of the kind usually sold during the life of the mortgage, or not sold in accordance with the custom or usages of trade, the mortgagor of course commits a fraud in taking advantage of his situation to part with the security belonging to the mortgagee. When the property is left in the mortgagor's possession his opportunity to wrong the mortgagee, if so inclined, is apparent. Suppose a mortgagor should be a dealer in costly jewelry or other goods left in his possession, and all the requirements

of the law are fulfilled with respect to recording the mortgage, nevertheless, it would be very easy for the mortgagor, were he so inclined to rob the mortgagee of a considerable part of his security before his discovery of the mortgagor's doings.

16. Such mortgages are frequently assigned by the mortgagee like a mortgage of real estate. This is usually effected by writing an assignment on the back and having this recorded in the same manner as the original deed. When this is properly done the assignee acquires quite as good a title to the debt and property as was possessed by the mortgagee.

17. On the maturity of several notes at different dates, secured by the same mortgage, the mortgagee may at his option take possession on the first default, if not in possession already, or he may await the maturity of the last note.

18. It is the mortgagor's own loss, should he neglect to pay the instalments as they fall due, and thus save a forfeiture of his property. All legal claim on the mortgagor's part is gone after forfeiture, and he cannot compel the mortgagee to receive payment and restore the property. Nor is the mortgagee bound, after taking possession because of the mortgagor's failure to comply with the mortgage, to make a sale unless the deed requires this to be done.

19. Equity looks with a favourable eye on the retention of possession by a mortgagor, and will do whatever is possible in the way of securing fair treatment from a creditor. Therefore, anything like fraud or harsh dealing on the part of a mortgagee, the taking

of the property without proper notice or by an unfair sale, will be corrected by a court of equity on the proper presentation of all the facts.

20. In foreclosing a mortgage, which is often done, the court proceeds in the same manner as with a mortgage of real estate, first fixing a time for the mortgagor to pay, and after his failure to do so, transferring all his right and interest in the property. When the property is sold, the surplus, should there be any, belongs to the mortgagor; should there still be a deficit he is liable therefor.

21. The payment of a mortgage debt to the mortgagee by some third party, who is under no obligation to pay, does not necessarily operate as a satisfaction. The intention of the third party in making the payment must be regarded. If it is his intention to preserve the debt the law will keep it alive. Whenever a mortgage debt is extinguished so is the mortgage security.

22. A ship may be mortgaged like other personal property and the national statute provides how this shall be done. In general it may be said that the mortgage must be registered like a mortgage of real estate and the methods of dealing with it are quite the same.

CHAPTER XXIV

PLEDGE OF PERSONAL PROPERTY

1. What may be pledged.
2. Natural increase follows the thing pledged.
3. Property should be delivered to pledgee.
4. When pledgor may retain it.
5. What care pledgor must take of it.
6. What use can pledgor make of it.
7. Pledgee may transfer his debt and security.
8. Pledgor's remaining rights.
9. Pledgor's bankruptcy does not affect pledgee.
10. Pledgor's consent is necessary to give pledgee good title.
11. Negotiable paper is an exception.
12. Collaterals:
    a.—Presumptively they belong to pledgor,
    b.—Is pledgor or pledgee liable for an assessment?
    c.—Does a pledge cover a renewal?
13. Rights of pledgee holding various collaterals.
14. Pledge of collateral security received from a third person.
15. Pledgor must pay or permit pledgee to sell.
16. Notice of sale.
17. Mode of sale.
18. Purchase by pledgee.
19. Balance due pledgor or pledgee.

20. Effect of subsequent agreement to accept collaterals in settlement.
21. Pledgor must pay expense of sale.
22. Pledgee may sue pledgor instead of selling property.
23. By paying debt pledge is extinguished.
24. Pledgor on payment of his debt may have his property.
25. Pledgee cannot divert property.
26. Effect of relinquishment by pledgee of collaterals on other creditors.
27. Pledges to pawnbrokers.

1. Personal property is often pledged for debts, and in setting forth the law relating to pledges, the first question is, what can be pledged? Almost every kind of personal property and rights of personal property, all kinds of merchandise and securities, shares of stock, bank-notes, mortgages, leases, patent rights, and the like. The principal exception is property not existing at the time of the pledge, though there may be a mortgage of future acquired property. It is contrary to the law to pledge some things—pensions, bounties to soldiers and sailors. The law guards the business of pawnbrokers, because they sometimes take property that ought not to be received; or take advantage of the situation of the pledgor to make unreasonable demands. Partnership property cannot be pledged for an individual purpose. A transfer of bonds belonging to a company by the president as collateral security for a pre-existing debt of his own is void, even if he were authorised to sell them.

2. In pledging a thing for a particular purpose the natural increase also follows and enures to the benefit of the pledgee. Thus, the young ones of a flock of sheep, which are the subject of a pledge, become a part of the flock. In like manner the dividends of interest on stock or other securities go to the pledgee, unless the agreement says otherwise.

3. Pledged property should be delivered to the pledgee. The reason is, the property that remains in the pledgor's possession is regarded by the law as still his, and may be taken by his creditors to satisfy other debts.

4. Many of the states provide by statute for the retention by the pledgor of his property, while granting adequate security to the pledgee. But it is contrary to the policy of the law to permit or sanction a secret transfer. This rests on a sound reason, that creditors may not be surprised or defrauded by the discovery that the possessor of wealth is not the real owner.

With respect to stocks, the law in some states, though not in all, provides that the delivery of a certificate to the pledgee, signed in blank, shall be a sufficient delivery of the property. The law requires nothing more than this transfer of the certificate to protect the pledgee's or purchaser's interest from the seller's creditors.

This transfer, if sufficient to protect the pledgee, is so solely by virtue of the statute. Consequently, all other property, not within the statutory ken, must be actually delivered to the pledgee in order to make his security complete.[1]

[1] For form of transfer of stock, see Vol. IV, Appendix, No. 25.

5. What care must a pledgee exercise over the property? The law has endeavoured to measure the care by the compensation received for the service. In keeping stocks a receiver or keeper who receives no compensation but simply does this for another's accommodation, need exercise a less degree of care than a person who is especially engaged in the business, and who receives a compensation therefor. For example, once it was a common practice of bank depositors to ask their cashier to keep their bonds or other securities and valuables for them in the bank's safe during their sojourn by the sea, or abroad. As this was a purely gratuitous service, losses by fire, robbery, or other cause, unless the bank was grossly neglectful, could not be visited on the institution. On the other hand, a bank with a safe-deposit department, or an institution engaged solely in the business of keeping securities for a compensation, must exercise the highest degree of care; is essentially an insurer; and is responsible for a loss by fire or robbery, unless it can prove the exercise of the highest degree of care.

A bank receives a direct pecuniary benefit from stocks or other securities pledged for a loan, and is obliged to exercise more than ordinary care in keeping them. Should a loss therefore occur through its negligence it would be obliged to recompense the pledgor.

6. What use can a pledgee make of a pledge? This depends on the reasonable intention of the parties. If the pledge consists of goods, stocks or other valuable securities yielding dividends and profits, or a herd of

cattle, the pledgee certainly cannot avail himself of the dividends or profits except to discharge, so far as these may go, the pledgor's indebtedness to himself.

7. The pledgee may transfer or assign the debt and security to other parties. He may deliver them into the hands of a stranger for safe custody, or he may convey his interest conditionally by way of a pledge to another person. In so doing his security is never destroyed nor impaired. On the other hand, by such an assignment or transfer he cannot affect in any way the rights of the pledgor.

It is true that some things cannot be assigned or put into the hands of another; for example, valuable paintings or precious stones. Just where the line runs is not always clear. In the way of a general principle, it may be said that a pledge, unless it contains a reservation, may be repledged to another.

8. The pledgor has some rights left in the pledged property. He may sell or assign it, subject to the rights of the pledgee. The vendee stands in the pledgor's place, can redeem the pledge, and hold the pledgee to account.

9. The pledgee's security is not affected by the bankruptcy or death of the pledgor.

10. There can be no valid pledge or transfer of title unless the owner has either expressly or implicitly assented to the transfer; merely because one happens to be in the possession of goods as their keeper gives him no power to pledge them for his own debt or engagement. Thus, should the bailee of a yoke of

oxen, in a fit of wickedness, pledge them as security for his debt to another, the true owner could recover them from the pledgee; indeed, from anyone to whom they might be sold by the pledgee or subsequent possessor.

11. To this rule must be noted one exception; the law prescribes a different rule for negotiable paper in order to give it freer wing. Sometimes the holder pledges it to another as security for a loan or other purpose. Such a pledgee, acting in good faith, not knowing that it belongs to another, acquires a good title. Though this is the rule, the courts often regard these transactions with suspicion. If there is any reason to suppose that the pledgee has some knowledge or suspicion that the notes, stocks, or bonds belong to another, he cannot hold them as against the true owner. Not infrequently a bank officer indulges in speculation, and to secure his loans, sends his broker stocks or negotiable securities belonging to the bank, or to its customers. The courts do not hesitate to uphold the loans and to preserve the title of the pledgee to the securities thus received in good faith by the broker without any suspicion attaching to them. But, we repeat, courts guard these transactions very carefully. The very office held by a bank official ought to be enough in some cases to lead a broker to suspect that he has sent other securities than his own. This is especially so for heavy loans and extending over long periods; especially in speculations or gambles that result disastrously to the officer.

12. Stock delivered as collateral (*a*) is presumed

to be the pledgor's own property, until the contrary is shown. The bonds of a customer, therefore, deposited by a broker as collateral security for his individual indebtedness, without any notice of their true ownership, may be retained for the loan. But their transfer by the pledgee to his own name by virtue of a power of attorney, as a precaution, does not destroy the pledgor's title.

(*b*) Some difficult questions have arisen in assessing collaterals. Who shall be assessed? The general rule is, the pledgee is the legal owner, and if the stock still stands in his name he is the proper person to assess. Sometimes he avoids liability by suffering the title to remain in the name of the pledgor. This is not always done, for the reason that the pledgee's ownership or control may be thereby imperilled. So he prefers to run the risk of loss through insolvency of the issuer than the risk through the pledgor's retention of ownership.

In assessing pledged stock, though the truth has been often shown that the pledgee was nothing more, he has often been required to pay the assessment. The courts have declared that the statute ordering the assessment was imperative, requiring the person having the *legal* title to pay, and, as this was held by the pledgee, he could not escape.[1]

It has therefore proved somewhat difficult to secure the pledgee on the one hand, and yet relieve him of liability to assessment for the indebtedness of the company issuing the stock, on the other. A satisfactory

[1] See Morawetz on Private Corporations, Chap. 1, § § 1, 32.

way has at last been found when the fact clearly appears that the stock is pledged simply as security, and that the pledgee does not intend thereby to be legal owner or holder, except to the extent of securing his debt. The law now looks at the real transaction in its true light, and subjects the pledgor to assessment.

(*c*) Occasionally the question arises whether collaterals given to secure notes may be kept to secure renewals and advancements. Of course, when a note is renewed on the security of a collateral security the holder is also a bona fide holder of the collateral. Furthermore, an alleged misapplication of collateral security is waived by giving a new note for the original loan without objection or abatement.

13. The pledgee may hold various collaterals and avail himself of any of them as long as the debt is unpaid.

14. Again, a creditor who receives collateral security from a third person is bound, on accepting it, to preserve the original debt, for in equity the third person, who thus delivers the security, is entitled to the original debt, as security for himself.

15. After the maturity of the debt the pledgor must pay, or the pledgee can acquire, a complete title to the pledge. Generally, the contract carefully prescribes what the pledgee must do with the security. It must be sold in a specified manner, usually by public sale, or within a prescribed period, or at the discretion of the pledgee, and the proceeds be applied to discharge the pledgor's obligation.

16. The notice of sale must be reasonable. As the

remedy is very summary, the opportunity to redeem is permitted to the last; or, if the debtor is unable to accomplish this desirable end, he may have the opportunity to secure the attendance of bidders to prevent the sacrifice of his property or of a collusive sale to interested parties.

17. The pledgee must faithfully exercise his authority. He is not bound to obtain the highest possible price, but is bound to exercise common business prudence and good faith. The temptation is often great to take advantage of his situation and obtain the security at less than its real worth. The law brands such action as corrupt and indefensible, and will promptly set it aside.

18. In many cases loans are made by banks on the pledge of stocks, bonds and other securities listed in the stock exchanges. The contract provides that, in the event of non-payment by the pledgor, the security shall be sold at open board in the market, thus preventing all possibility of committing any fraud on the pledgor. Consequently there are fewer cases of fraudulent dealings with pledgors than formerly.

In perhaps all the states there are statutes regulating the mode of selling pledged property; of course these must be followed wherever they exist.

A creditor who sells collaterals at public sale, and buys them for himself, holds them as he did before, as security only. A judicial sale only, or the right reserved to purchase, will destroy the equity of redemption.

19. For a balance still due by a pledgor after the

sale of his security, he is liable; should there be a balance in his favour the pledgee must return it to him.

20. Sometimes it is impossible for the pledgee to sell the securities at a price equal to the debt, and he makes a subsequent agreement to take them in full discharge of the pledgor's indebtedness. By such an agreement of course the pledgee's title to the property is complete; should its value afterward increase the pledgor has no further claim or right of redress against the pledgee.[1]

21. The necessary expenses of selling a pledge are chargeable to the pledgor. But when an instrument describing the terms of a pledge also provides for its sale and the application of the proceeds to the payment of the debt, "and all necessary expenses and charges," the counsel fee for the trial of a cause pertaining to the instrument itself is not included.

22. The pledgee may sue the pledgor instead of enforcing the security. The pledgee must, however, fulfil the conditions of his engagement and sell the property, provided the contract requires such action.

23. A pledgor is entitled to a restoration of his property whenever he has fulfilled his part of the agreement, or offered to fulfil it. On tendering the amount due at the appointed time the pledgee must surrender the property or become liable for its conversion unless he can show a good reason for his denial. Nor is the debtor's unwillingness to pay the debt of another person any justification for retaining the property.

24. What, then, is a diversion? A pledgee cannot

[1] For form of assignment see Vol. VI, Appendix, No. 16.

deliver a collateral security to another, nor can it be held as security for subsequent advances.

25. A pledged security must be returned on payment of the debt.

26. A pledgee may relinquish collateral security given him by his debtor, regardless of the consent of other creditors, without losing his right to proceed against the debtor's property. And when money is advanced after the sale of the property pledged, the claim of the advancing creditor is not affected by the action of the pledgee in parting with the property.

27. Pledges to pawnbrokers have been regulated by many of the states. The pledgor's condition for money often leads pawnbrokers to exact excessive rates of interest or security; consequently the states have regulated more strictly their business than that of banks and other money lenders.

By the common law goods pawned or pledged and in the pledgor's possession cannot be taken by a pledgor's creditor. This is the rule everywhere, so long at least as the pledgee's title or interest remains unextinguished.

CHAPTER XXV

RIGHTS OF LIENORS

1. What is a lien.
2. Equitable lien.
3. Statutory lien.
4. Particular and general liens defined.
5. How a particular lien is created.
6. How a general lien is created.
7. A lien cannot arise from one's own wrong.
8. Lien of a carrier.
9. Warehousemen:
    a.—Defined,
    b.—How lien is created,
    c.—His receipt for property received,
    d.—What receipt contains,
    e.—Is not negotiable,
    f.—Except by statute,
    g.—Warehousemen cannot impeach it,
    h.—He can insure property.
10. Wharfinger:
    a.—Wharfinger defined,
    b.—His responsibility for goods,
    c.—Notice of delivery to him.
11. Factor.
12. Banker.
13. Attorney.
14. Innkeeper:

a.—Compensation,
b.—Lien on minor,
c.—Lien on property of others in a guest's possession,
d.—Lien on animate property,
e.—Mode of selling property to satisfy lien,
f.—How lien may be lost.

15. Boarding-house keeper.

1. A LIEN is a claim of a person on the property of another, as a security for some debt or demand. The right to hold or retain property by lien lasts until the debt or demand is secured.

2. The law recognises various kinds of liens. One kind is an equitable lien, of which mention has been made when treating of the law of the sale of real property.

3. Another lien is known as a maritime lien, and has been considered in another place. A third kind of lien is known as statutory, and this plays an important part in modern law. Statutory liens of various kinds have been established, but the one with which all are most familiar is known as a mechanic's lien, whereby mechanics, workmen on buildings, as well as those who furnish the materials used in constructing or repairing them, have a lien thereon for the value of their materials or services. Another kind of lien is known as the common law lien, which is the most primitive of all. It is a legal right to retain possession of the thing to which it pertains until the debt or charge is paid.[1]

[1] For form of notice of mechanic's lien see Vol. VI, Appendix, No. —.

4. The common law lien is again divided into general and particular. A general lien is a right to retain another's property for a general balance of account. A particular lien is the right to retain property on account of labour and expense bestowed on that identical property. Such a lien has long been favoured in the law. Common carriers, innkeepers, attorneys and the like have a particular lien.

More generally every bailee for hire who has added value to goods by any service has a lien thereon to a reasonable amount. The lien extends to all trades or occupations—tailors, dyers, millers, wharfingers, warehousemen and the like. One who keeps and trains a race-horse has a lien thereon for keeping and improving the animal. But neither a livery-stable keeper nor a cattle-keeper has a lien on animals delivered to him for keeping without a special agreement. By statute the lien exists in some states.

Custom is sometimes quite important in determining the nature and extent of a lien. A particular lien may be created or destroyed by agreement.

5. Particular liens can be created by express contract. They also exist under some circumstances. While the finder of lost property on land, unlike the finder of maritime property, cannot claim a lien for taking care of it for the loser, yet a finder who is promised a reward for his discovery has a lien on the property for his service.

6. A general lien, like a particular lien, may arise by express agreement. Carriers and innkeepers occasionally try to limit their responsibility, and increase

their lien security by general notice, but the courts are not inclined to favour these departures from ordinary methods.

7. A lien cannot arise from one's own wrong; for example, on a certificate of stock held through a breach of trust. Nor can the owner be deprived of his property without his knowledge or consent, personally or through his agent.

8. The lien of a carrier covers the goods he carries, and unless he has made a special contract to deliver them before receiving payment for his service, he can retain them until the charge is paid. The lien also covers advances to others for freight and storage on the goods; but it does not include former unpaid charges, nor any other indebtedness. He also has a lien on the baggage of a passenger for his fare, but no lien on the passenger himself.

9. (*a*) Warehousemen have been defined to be persons who receive goods and merchandise to store in warehouses for hire. The persons who follow this business of storing grain, furniture, etc., have a lien thereon for the service they render.

(*b*) To create the lien, as in other cases, the property must come fully into the possession of the warehouseman, so that it may be controlled by him or by his agent. It need not be actually in his warehouse, but it must be on his premises and under his control.

(*c*) On receipt of the property the bailor should deliver to the owner a receipt for the same. No particular form of receipt is required; usually it contains the date of the property received, a description, from

whom, and an agreement to redeliver on demand to the bailor or to his order.

(*d*) It is quite common for the receipt to contain an agreement providing how the property shall be kept and the amount to be charged, also that a lien shall exist thereon for the payment of the services rendered. This agreement or stipulation is, in truth, a real contract. Many persons have taken these receipts, thinking or believing they possessed simply this character. They have often proved to such persons to have been costly delusions. On numberless occasions the courts have declared that they were contracts, binding on both parties, and relieving warehousemen from any risks or liability which the bailor had innocently supposed the other had assumed. The chief limitation placed on shipping receipts by the courts is exemption from negligence, no matter how specific the stipulation may be. In some states, notably New York, even this rule has been relaxed and bailees may exempt themselves from all liability whatever by an express contract founded on a proper consideration.

(*e*) A warehouse receipt is not a negotiable instrument, except by statute. Nevertheless it is often indorsed and a certain kind of negotiability is attached thereto. It is often pledged as security for a loan.

Again, it is often transferred as if it were a negotiable instrument; nevertheless, technically it is not one; yet on the delivery of such a receipt to a bank as security for a loan, the title of the property therein described is transferred as effectively as it could be by the actual delivery and retention of the property itself.

(*f*) By statute in many states a warehouse receipt is made negotiable. The statutes provide that it may be transferred by indorsement and delivery, that the indorsement may be either in blank or to the order of another, and shall be deemed a warranty that the indorser has a good title and lawful authority to sell the property named therein. It also provides that the transfer of the property by negotiating the receipt shall be subject to a lien of the warehouseman for charges and advances.

(*g*) A warehouseman is not permitted to impeach his receipt. He is not permitted to show that the property received was not of the kind represented. If he did not know it was his duty to ascertain the truth before receiving the property. It would be a dangerous principle to permit him to set aside his own authority or warranty unless he could show that some fraud had been practised on him.

(*h*) A warehouseman has an insurable interest in the property confided to his care. Justice Gray has declared that "by the law any person has an insurable interest in property by the existence of which he receives a benefit, or by the destruction of which he will suffer a loss, whether he has or has not any title in or lien upon or possession of the property itself."[1]

10. A wharfinger maintains a wharf for receiving goods for hire. (*a*) His duties and liabilities are not unlike those of a warehouseman. Like him, he is liable for any loss happening through his neglect to exercise ordinary diligence.

[1] Eastern Railroad v. Relief Fire Ins. Co., 98 Mass., 423.

(*b*) He cannot be charged with responsibility for goods until they are put within his control. A mere delivery of them at the wharf is not necessarily a delivery to the wharfinger. The usages of business are important to show when he acquires and ceases to have the custody of merchandise.

(*c*) In some places the usages of business require that he should be notified of the delivery of the goods to him; in truth, this usage is very general.

11. A factor or commission merchant is also a bailee for he has the custody of the property he is authorised to sell. He must use ordinary diligence, and consequently is liable for ordinary negligence. He must exercise good faith in caring for the property and performing his duty as bailee. He can sell the property, but is not authorised to pawn, pledge or mortgage it. He guarantees to possess the skill and ability of ordinary factors; his liability, therefore, is not ended simply by exercising good faith.

He must follow implicitly the directions of his consignor. If there are none then he must take good care of the property and dispose of it as the general usages of trade require.

A factor, unlike a broker selling in the name of his principal and without possession of the property, has both a particular lien and a general lien for the balance of his general account on all the debtor's goods which remain in his hands and are subject to his control. The lien extends even to the price of the goods which the factor has sold, though he has parted with their possession. It may extend to all sums for which he has

become liable for his principal or otherwise by virtue of the relation between them. The doctrine also applies to purchasing as well as to selling factors. Usually the lien of a factor prevails over an attachment by a creditor. If he has sold part of the goods he is entitled to a lien on the residue for his expenses, advances and commissions. The general lien applies only to goods received and not simply to consignments.

12. Bankers also have a general lien on the securities of their customers or on their deposits for any general balance due from them.

13. Attorneys and solicitors also have a general lien on the papers of their clients in their possession for the general balance of their professional accounts. They also have a lien on the moneys recovered in a particular action. The law is liberal in dealing with them and provides for their protection so far that not only fees and disbursements in a particular suit may constitute a general lien on the moneys recovered in such suit, but other fees and disbursements in any other suit covered by the same retainer.

14. (*a*) The lien of an innkeeper is on all the property brought within the inn by a guest or put in the innkeeper's custody. The amount of compensation he may demand, and secure by his lien, depends on the general usage of the business in this city or other place. The amount includes the reasonable charges of friends of the guest who have been invited by him, as well as extras in the way of wines, cigars, etc.

(*b*) A guest who is a minor is liable only for neces-

saries. Should he order wine suppers and extravagant extras the innkeeper would have no lien on his clothes or baggage for furnishing them.

(*c*) In England the question has been much considered whether an innkeeper has a lien on the property of third persons in the possession of a guest, put by him in the temporary possession of the innkeeper. By the American rule innkeepers have a claim only on the property belonging to the guest himself. Judge Thompson says that "American courts have not hesitated to declare that a common carrier has no lien for the carriage of goods which he has innocently received from a wrong-doer without the consent of the owner, expressed or implied." He also adds, "We are satisfied that a lien of a hotel or innkeeper does not exist in such a case. We are not prepared," he continues, "to agree with those courts which have found a plain principle of justice in the rule of law by which one man's property is confiscated to pay another man's debts."[1]

The foundation of the English rule is the service rendered in protecting the goods received by the innkeeper regardless of the person who has brought them. The courts say that, for the service thus rendered, there should be a recompense, whether the possessor was the owner or the possessor of another's property. Is not this a sound foundation for the English rule?

When a guest is a servant, agent or bailee of the owner and engaged in his business—for example, a travelling salesman—and carries his goods into the

[1] Wyckoff v. Southern Hotel Co., 24 Mo. App., 382, 390, 391.

inn and puts them into the innkeeper's custody, the innkeeper has a lien thereon for keeping them.

(*d*) Likewise an innkeeper has a lien on animate property—horses or other animals—taken to his inn by the agent or servant of the owner in transacting his business, for the animals must have keeping and care and their owner derives a benefit from the innkeeper's service.

(*e*) In almost all of the states the lien of an innkeeper on the goods of his guests for compensation is regulated by statute. They also provide for the mode of selling them and satisfying the innkeeper for his services.

(*f*) In several ways an innkeeper may lose or waive his lien. First, by tendering to him his property charges; second, by his refusal to deliver the property on other grounds than that of non-payment of his compensation and his lien on the goods; third, by his agreement to give credit to the guest, for this would be inconsistent with the enforcement of the lien.

If an innkeeper once parts with the possession of his property voluntarily, or loses or waives his lien it cannot be revived by regaining or assuming possession.

15. Lastly the right of a lienor does not extend to boarding-house keepers, because they are not required to receive guests, like hotel or innkeepers. The latter are engaged in a public duty; boarding-house keepers are not. But by statute, boarding-house keepers in some states have the same rights as innkeepers.

CHAPTER XXVI

BAILOR AND BAILEE

1. Definition.
2. Contract must be for a legal purpose.
3. Who can make a bailment contract.
4. What property can be bailed. Must be put into bailee's possession.
5. Bailor need not be absolute owner. He may be a thief.
6. What bailor can still do with property.
7. Bailor must tell bailee of its condition.
8. When is the transaction a sale and not a bailment.
9. Bailments classified.
10. Object of classifying.
11. What care bailee must exercise:
    - *a.*—Care required of one not receiving a reward,
    - *b.*—Every case must be judged independently,
    - *c.*—Classification of decisive circumstances,
    - *d.*—Rule applicable to bailor who knows that bailee is negligent with his own property,
    - *e.*—Care must keep pace with improvements,
    - *f.*—Contributory negligence by bailor.
12. Bailee's right to use property.
13. Bailee's right to recover property when taken from him.

14. How a bailment may cease.
15. What skill must be rendered.
16. Bailee must return property after performing the object of bailment.
17. When specific property need not be returned.
18. Excuse for non-return.
19. Bailee's lien.
20. Bailee's lien when he is a finder.
21. Bailee may assign property.
22. Rights of parties when bailee adds to the value of the property.
23. When is the transaction a bailment or partnership.
24. Consequences of loss by fire, etc.
25. Failure to do work properly:
    a.—When the bailee can recover partial compensation,
    b.—Effect of abandonment by bailee,
    c.—Bailee can recover when bailor is at fault,
    d.—Failure to perform through inevitable accident.
26. Bailee may do the work by agency of others. Exceptions.
27. When the bailor must make his claims for damage.
28. Cold storage.

1. Let us begin with a definition. Story's perhaps is more frequently quoted than any other. It is, "A delivery of a thing in trust for some special object or purpose and upon a contract, expressed or implied, to conform to the objects or purposes of the trust."

2. The contract of bailment must be for a legal purpose; were it for any other the law would not recognise the relationship or protect either party seeking to enforce the contract.

3. Any person who is competent to make a contract may become a party to a bailment. While an infant or married woman could not, at common law, make such a contract yet if property should come into her possession, the law would require her to exercise proper care of it; she could not destroy, injure or misappropriate it. A minor who should hire a horse and carriage to drive to a place, and, without authority, should drive beyond and rashly, killing the horse, would be liable for the value of the property thus wantonly destroyed. A corporation may become a bailor or a bailee. From its very nature it must act through officials or agents. And an agent, unless acting wholly beyond his authority, may create a bailment relation for his principal.

4. To create the relation of bailment the property must be of a nature capable of delivery to the bailee. Furthermore, there must be a delivery on the one side and an acceptance on the other.

While this is true in most cases, it occasionally happens that property comes into the possession of a bailee in other ways. One may find property—a pocketbook, for example; the happy finder is by no means the owner, simply a bailee for the owner. In this case no contract exists except the one implied by the law that the finder may retain the thing and exercise due care in keeping it. What his duty may

be in the way of trying to find the owner will be considered hereafter.

5. A bailor need not have an absolute title or ownership of the property. He must have a possessory right to the thing; having this he can give its care and custody to another. A bailor, for example, may simply be a lessee, yet he would then have the rights, under some conditions, of keeping the property, previously in the possession of the lessor, as bailee.

As bailment is founded on the right of possession a thief may make a bailment of stolen property. Furthermore, if the owner does not interfere, the thief may recover the bailment, should the bailee, on the termination of the relation, refuse to deliver it. A bailee cannot destroy a bailor's title.

6. The bailor can sell or encumber property while in the possession of the bailee. He may mortgage it, or in any other way encumber it and the bailee must respect the rights of the purchaser or mortgagee.

7. It is the bailor's duty to exercise good faith toward the bailee in giving him notice of all the faults inhering in the thing bailed which may expose the bailee to danger. For example, it would be the duty of a bailor, who should loan a vicious horse, to notify the bailee of his bad character. Should the bailor fail to do so he would be liable for the consequences.

8. The question has sometimes arisen whether the transaction is a bailment or a sale. It would seem as though this question ought to be common in everyday business, because the two contracts are so different in their nature; nevertheless the courts are occa-

sionally required to answer this question. If the identical property is to be returned, or the same property in a changed condition, or the natural product of the same property, the transaction is not a sale. One well-known test, says Benjamin, between a bailment and a sale is that when the identical thing delivered is to be returned, though perhaps in an altered form, it is a bailment and the title is not changed, but when there is no obligation to return the specified article received, and the receiver is at liberty to return another thing, either in the same or some other form, or else to pay money, he becomes a purchaser. Thus, when casts were delivered to be manufactured into shears, the plates to be furnished by the bailee, this was held to be a bailment.

9. Much difficulty has arisen in classifying bailments. For our purpose, however, we will divide them into three classes. First, things delivered to a bailee purely for his accommodation; second, things purely for the accommodation of the bailor; third, things for the benefit of both parties. Examples may be readily enough furnished of each transaction. A person, for example, borrows a knife of another or some utensil for his own individual use. This is loaned to him not for any reward, but purely as an accommodation. Again, a bond received by a bank to keep for a depositor for which no compensation is expected or paid is a bailment of the second class. An example of the third class may be given of cattle which are put for safekeeping into the possession of another, who is to be paid for the service rendered.

Both parties are the gainers, and this is their intent in changing the possession of the cattle.

10. The chief importance of classifying bailments is to determine the degree of care that should be exercised by the bailee in keeping them, for evidently, when a bailee is not to receive a reward, the act being purely gratuitous on his part, a much less degree of care is required than when the opposite conditions between the parties exist. Thus, a safe-deposit company, established to receive deposits and receive a reward for its service, must exercise the highest degree of care in keeping them. A bailee may greatly lessen his liability by special agreement; indeed, in some states, may be entirely released.

11. From the earliest days there has been the greatest difficulty in determining what degree of care should be exercised in these matters. About the only line of agreement is, that a less degree of care is required of a bailee who is to receive nothing for the service than of one who is to be rewarded. But where shall the line between the different classes be drawn?

(*a*) Perhaps a statement more frequently reiterated than any other is that a bailee who serves without reward ought to exercise the same degree of care that is exercised by a prudent man in keeping a thing of his own of a similar nature. Assuming this rule to be correct, then the question in every case is, do the facts come within it rendering a bailee liable, or not? Consequently every case must be determined by itself and the law can impose no rule the application of which is always the same, or self-evident. In

other words, the rule of law, whatever it may be, is one of varying difficulty in its application, because the facts are dissimilar pertaining to the bailment.

This may be illustrated in the keeping of securities by banks for their customers. As is well known, it is a common practice of banks to accommodate their customers in this way, especially country banks, where safe places for keeping things are not as numerous as in the large cities. Every now and then bonds or other securities have been lost or taken and the bailor has sought to recover from the bank. How have the courts decided? Generally they have told the jury that they must apply the rule above mentioned, and then left them to decide whether, in the light of this rule, the bank was negligent or not.

A bank is no more responsible for a loss by the theft of one of its employees than for a loss occasioned by an unknown person. This may seem a hard doctrine, but its reasonableness will soon appear. A famous case occurred in Massachusetts many years ago of the loss of a keg of gold stolen by the cashier. The fact was clearly enough proved that the cashier had stolen it, and the bailor tried to hold the bank responsible therefor. The court said nay, declaring that the cashier was not employed by the bank to steal, and therefore it could not be held liable unless it had some reason to doubt his honesty or integrity. If a bank should employ a servant whose honesty was suspected then, indeed, it would be responsible for the consequences, not otherwise. Everywhere a bank seeks to employ only trustworthy servants, and

if it is occasionally misled it is free from responsibility to an ordinary bailor who has given no reward or recompense to the institution for keeping his securities.

Such is the ordinary rule. Attempts have been made to show that the profits derived from keeping a depositor's account are a sufficient consideration for a contract of bailment to which a more stringent rule of liability may be applied. The courts have lent no countenance to this contention, and so the rule of law everywhere is that such bailments are of a purely gratuitous character, and the bank is not liable for their loss when exercising ordinary diligence.

(*b*) The latest authority on the subject has remarked that every case must be ruled by its own facts and circumstances. The advent of every new invention, the discovery of every new and important force that is appropriated by man and made subservient to the great on-marching industries in these days of progress, bring with them new and varied circumstances and conditions which must be considered in defining and determining what is negligence and what is diligence in a given case.

(*c*) The circumstances that may be decisive of the care exercised by a bailee may be thus classified: First, the nature and value of the article; second, the customs of the place of trade; third, the conditions of the country or climate; fourth, the condition of the times.

Of the first class of cases it may be said that one

in charge of heavy and immovable articles would not be deemed guilty of negligence should he leave them out of doors unguarded overnight, while a very different rule would apply to a jeweler who was acting as bailee of valuable diamonds and precious stones. Again, the customs or place of trade are often valuable signs or guides for determining the degree of care that should be exercised by a bailee.

(*d*) While the rule of ordinary diligence applies in all cases, and a much stricter rule when a consideration is paid for the bailment, an exception must be made in cases wherein the bailor knows that the bailee is neglectful concerning the management of his own property. When a bailment is gratuitous, and the bailor knows of the bailee's way of doing business, it is not rational to suppose that he will exercise a higher degree of care of others' property than of his own. In such cases therefore a still lower level will suffice to fix the liability of the bailee. It is true that the courts are not uniform in their application of rules, some of them holding that while a person may be negligent in managing his own affairs, he should not be when managing the affairs of another, even though he is to receive no reward for his service.

(*e*) Again diligence must keep pace with improvements; and though dangers thicken with civilisation, so do the means improve of preventing losses, and these must be utilised to overcome danger. A recent authority has remarked that a custodian for hire is bound to keep pace with the advanced requirements and practices of his class. If he does this he es-

capes liability for loss or injury that comes to the property entrusted to him; if he does not he has failed to be ordinarily diligent and is liable for the damages that result through his failure. It is true that a bailee is not obliged to adopt the very best and newest appliances to secure the protection of his customers, but he must be ordinarily prudent in their use.

(*f*) Sometimes the bailor himself has been negligent in caring for the thing lost or injured. In such cases clear proof of his contributory negligence may be a good defence to an action for the loss or injury of his property.

12. In using the property the general rule is a bailee must act simply as a keeper. To this rule there are some exceptions. Thus, were a milk cow put into the possession of a bailee, it would be his duty to have her milked; or a flock of sheep near shearing time, to have them sheared.

The law implies that the bailee will put the property to its natural and ordinary use, and if in so using it, he is put to expense, the bailor is required to reimburse him. For example, the natural use of a horse requires the feeding and shoeing of the animal, or, if taken sick, attention by a veterinary. When these things are done the expense must be refunded by the bailor.

Should the bailee use the property confided to him in an unwarranted manner he would be liable therefor. What this may be of course depends on his use of it. Sometimes the contract of bailment prescribes how the property may be used or kept. For exam-

ple, to put a fine carriage team, left with the bailee for the purpose of pleasure driving, to the plow or to hard work on a farm, would be an unauthorised use.

13. The bailee only has a possessory title to the bailed property. Nevertheless he can bring an action for its recovery should it get out of his possession, or trover for its value.

14. A bailment may cease in several ways. First, by the expiration of the time for which the property was bailed; second, by the attainment of the object for which the bailment was made; third, by demand on the part of the bailor; fourth, by operation of law; fifth, by destruction of the bailed property; sixth, by the death of the bailee; seventh, by the incompetence of either party to continue the relationship. For example, should the bailee become insane or habitually drunk, or otherwise unfitted to exercise the duties he has undertaken.

15. Although the bailee is to receive no compensation, he must render the kind of service concerning the thing bailed which he holds out to the public he is competent to perform. Thus, a skilled watchmaker who receives a watch for repairs, even though he has promised to do the work for nothing, must render the service he is capable of rendering; to do otherwise would be gross negligence. This rule is of wide application. The skill must be proportioned to the kind of work required. Thus, a painter or a diamond cutter must exercise the skill of a person in that particular capacity, and the law will be satisfied with nothing less. This principle has sometimes been applied

to dressmakers in which they have sought to employ others less skilled than themselves in the making of garments. In such cases, wherein the personal skill and attention of the person was supposely employed, the law is not satisfied either by trusting the work to another or by exercising less skill and ingenuity than is customarily exercised by the particular person or persons who do such work.

16. It is the duty of the bailee, after accomplishing the object of the bailment, to return the property to the bailor, or to a person designated by him, with all accessions thereto while in his possession. If the bailee refuses to do this without legal excuse the law regards him as having converted the property to his own use; and the bailor can either recover the value thereof, or bring a specific action, replevin, to recover the property itself.

17. The bailee has the right to the possession while the bailment continues; afterward the bailor has a reversionary interest in the property; he is entitled to its redelivery at the expiration of the contract in as good condition as it was at the time of taking possession, with due regard to the ordinary results of keeping. It follows, therefore, that the bailor has a right to defend his title of the property and to sustain an action against third persons, and even against the bailee for any trespass or use that is injurious to the property, which may depreciate its value or cause its destruction.

It is true that in many cases the bailee is not required to return the specific property, but may return

other property of the same kind and quality. Thus, wheat may be put into a common receiver, an elevator, and the contract of bailment is properly executed by delivering to the bailor at the required time wheat of similar quantity and quality. Again, wheat may be delivered to a mill to be made into flour, and the contract is properly performed by delivering to the bailor the proper quantity of flour of the same grade or quality as would have been manufactured by using the bailor's specific grain.

18. For the non-return of the property there may be some excuse; it may have been destroyed or lost without the bailee's fault. Again, it may have been delivered to another who proved himself to be the true owner; or again, the bailee may have been deprived of the property by due process of law, and therefore could not deliver it to the bailor. But if the bailee has no valid excuse of his own, on the expiration of the term of bailment it is his duty to deliver the property in proper condition.

19. The bailee has a lien on the property for his services. In many cases the compensation is fixed by agreement or law; in these there is no implied agreement or lien for compensation. In other words, an express agreement supplants the lien created by law.

The bailee, though having a lien on the property bailed, for its care and preservation, has no security for any other debt or obligation due from the bailor; the lien is confined exclusively to the care of the particular property in his charge.

Even if there be a mortgage on the property at the time of the bailment, a bailee's lien may have priority. This is true in those cases wherein it is necessary to repair the property in order to preserve it and render it useful. In other words, necessity creates a prior lien. Thus, on one occasion it was necessary to repair a canal boat, otherwise she would have become valueless. The bailee did so and the court held that he had a prior lien over the mortgagee for the expense thus incurred. The court remarked that the mortgagee having allowed the owner to continue in the apparent ownership of the boat, making her a source of profit and a means wherewith to pay off the mortgaged debt, the relation was created by implication entitling the owner to do all that might be necessary to keep her in an efficient state. It was as much to the advantage of the mortgagee as to that of the mortgagor or owner to have the repairs made and the boat preserved for navigation, and so the bailee's priority of lien prevailed.

20. A finder who lawfully comes into the possession of property becomes the bailee; and if he bestows any labour thereon, in good faith, which is essential to its preservation, he has a lien for the service thus rendered. It would seem as though an owner ought to be willing to make compensation in such cases, but the world is full of mean people, and so this question has arisen and has been thus answered. In one of the cases a boat was found adrift with holes in the bottom and in danger of sinking. The finder made such repairs as were needful to keep

her afloat, nevertheless the owner was unwilling to pay for them. The court decided very properly that as they were necessary for the protection of the property, the owner must pay before he could demand his boat.

21. A bailee under some circumstances has a right to assign the bailment to another. This rule has only a limited application, for in most cases the bailment is a confidential relation, one of trust, that is made because of the known character and fitness of the bailee. One of the cases in which this can be done is in subletting a lease whereby the farming implements and stock on the farm go to the bailee.

22. On many occasions materials are put into the possession of another for the purpose of having work done on them. Thus, a man delivers hides to another to be tanned into leather. The tanner is to use his skill in converting the hides into leather, and in so doing exercises an important part in giving additional value to the materials. Important practical questions have arisen concerning the ownership of such property and we will state the rules governing the parties to such arrangements.

While there is no fixed or settled rule respecting the proportion of the material the bailor or employer must furnish in order to establish the bailment relation, it is admitted that he must furnish the principal part of the materials to establish such a relation between them.

In these cases the bailee has a special property in the thing bailed, because he mingles with the prop-

erty of the bailor other materials and labour of his own and thus becomes a kind of part owner as well as actual possessor and creator of the property. This situation of the two parties renders the relation peculiar, giving the bailee a larger right or interest in the property than in other property wherein the bailee has no especial interest in the way of improving or creating it. Hence it follows, that as the bailment advances, the interest of the bailee must increase in value, consequently he may maintain an action to recover the value, or replevin to recover the property itself against one who deprived him of it, whoever he may be.

23. Sometimes in thus producing a thing jointly that is to be sold in the market, followed by a division of the net profits, the question has arisen, is the relation between the two a bailment or a partnership? In a recent case a court in New York held that the relation was that of bailment.

When no express contract exists to determine the rights of the parties, a recent and excellent writer has said that the law has established the following principles:[1] First, the bailor must do everything consistent with the employment to be performed on his part to enable the workmen to execute the engagement; second, to pay for all necessary and new materials; third, to pay the price or compensation that is to be paid for the work as agreed; fourth, to accept the thing when it is finished. On the part of the bailee the law requires: First, that he should receive, care for and

[1] Van Zile on Bailments, § 137, p. 83.

keep all material furnished until the contract is carried out or is terminated; second, to perform the service in good faith and as required by the undertaking; third, to do the work and produce the result of the undertaking within the time agreed; fourth, to use the skill and judgment required and which the workman promised to use upon the subject matter of the bailment; fifth, to use and employ the material in the proper manner; sixth, to exercise good faith and honest dealing in carrying out the undertaking; seventh, to exercise that degree of diligence in all forms of the service and in using the material and accomplishing the object of the undertaking that is required by law in such like cases; eighth, to deliver the property to the bailor when the bailment contract is fulfilled or otherwise terminated.

24. If the thing is destroyed during the execution of the agreement, who is the loser? Should the property be destroyed at any time by reason of internal defects, inevitable accident or irresistible force, outside the negligence of the bailee, or his workman, the loss would be the bailor's. The reason is because the property at the time of the loss is that of the bailor with all the labour and new material added. It therefore follows that the workmen would be entitled to recover from the bailor compensation for the labour he had bestowed on the materials to the time of its destruction.

The rule would be very different if a workman furnished all the materials and all the labour and was to produce for the employer manufactured articles.

In such a case were they destroyed in process of manufacture, or after their completion and before delivery, the workman could recover no compensation from the employer for his labour and materials for the very good reason that the property would not belong to the purchaser, but wholly to the workman.

Justice Story has thus stated the rule: "If the work is independent of any materials or property of the employer, the manufacturer has the risk and the unfinished work perishes to him. If the bailee is employed in working up the materials or adding his labour to the property of the employer, the risk is with the owner of the thing with which the labour is incorporated."[1]

Suppose there is a contract to do work at a stipulated price for the entire undertaking, and that the thing should accidentally perish or be destroyed, without any fault on either side, before the completion of the work. Would the workman be entitled to compensation *pro tanto* for his work and labour done and materials applied to the time of the loss or destruction? By the common law the workman is not entitled to compensation. The thing would perish to the employer and the work to the mechanic, for the contract would be treated as an entirety.

25. Of course a bailor is entitled to have the work done as the contract requires, and the bailee's failure raises no liability for compensation. If the parties stand in the relation of vendor and vendee it is the latter's duty to reject the goods because the vendor

[1] Bailments, § 426.

has failed to carry out the agreement. But he must act promptly, and refuse the goods, or express his dissent at once, and thus enable the vendor to protect his interest.

(*a*) There are some contingencies under which the bailee's failure to perform his contract does not deprive him entirely of compensation. If the work is so badly done that the product is of no value nothing can be recovered. If, on the other hand, the thing produced is of some value, even though it be imperfectly and ineffectually done, the workman can recover what it is actually worth to his employer.

(*b*) The cases are quite numerous in which the workman abandons his undertaking before completing it and his employer suffers a serious loss. The rule that applies in such a case has two sides or faces. If the workman has done something for his employer having a real value, notwithstanding his breach of contract, he can recover for the work and his service. Of course, there can be no recovery on the contract, for as this has been broken, the law does not recognise it in any manner whatever. It simply permits him to recover for what he has done possessing value to the other, regardless of the contract.

On the other hand, if the workman on thus quitting his undertaking has subjected his employer to a positive loss, far more than the worth of his service, the employer can recover to the full amount of the injury he has sustained.

(*c*) If the failure to perform is the bailor's fault, of course the bailee is entitled to recover for the worth

of his service. Thus, should an agreement call for the furnishing of more material, and the bailor for some reason or other fail to furnish it, whereby the bailee could not finish his undertaking, or not within the stipulated time, he would have his remedy against the other for his failure to execute his part of the contract.

(*d*) Again, a workman who is prevented by reason of inevitable accident from finishing the contract, and is in no way at fault himself, is excused, and cannot be deprived of compensation to a reasonable extent for the worth of his labour. In such case the bailee must show that he exercised ordinary care and diligence to avoid the accident which prevented him from completing the contract.

26. Generally speaking, a bailee may perform the labour expected of him through other persons, except those undertakings wherein the nature of the employment requires the skill of the person employed. For example, were an eminent artist employed to paint a portrait, he could not employ as a substitute an ordinary whitewasher. There is not much difficulty in applying the rule in these cases, as the nature of the work shows very clearly what can be delegated to others, and what not.

27. The bailor's claim for the loss or damage must be made immediately on their delivery by the bailee. In a recent case a manufacturer sent silk braids to a dyer to be dyed. After this was done the braids were returned to the bailor who wove a part of them in the ordinary manner. A short time afterward the

braids were found to be of greatly inferior value, which was due to unskilful dyeing. The dyer on returning the dyed silk sent his bill for the same on which was printed the following notice: "All claims for defects or damages must be made three days from date, otherwise no allowance." No notice was given by the manufacturer to the dyer until several months after receiving the notice. The court decided that he had not acted promptly enough, notwithstanding the imperfect character of the dyer's work, to claim compensation.

28. In closing this chapter some principles may be added that apply to cold storage, a business that is now rapidly growing in importance. A cold storage company is a bailee and, unless a special agreement exists, it must exercise ordinary prudence in preserving the merchandise entrusted to its keeping. Its nature and value also affect the question of care that must be used.

If the company's stock of ice or other means employed to maintain the temperature required for the preservation of the property is insufficient, it must replenish the supply, or give timely warning to its customers to remove their property. If neither thing is done the company is responsible for the injury caused by its neglect.

A cold-storage company is liable for damages to eggs resulting from the escape of ammonia, or from the gases emanating from fruit stored in an adjoining room, or from a rise of temperature caused by the melting of ice and neglect in replenishing the supply.

Fruit is often stored, and its preservation depends on keeping the storehouse at a proper temperature. Consequently, if the temperature is greatly lessened and the fruit is frozen, the bailee is liable; or, if it is ruined by keeping the temperature too high. And this is said to be the law even when decay is due in part to the condition of the property at the time of storing it. The bailee's storehouse should be properly constructed for the purpose; and, if it is not, he is responsible for the consequences. And this principle may be applied to a bailee, even if the bailor knew that its construction was faulty, or had time to make an examination for himself and did not.

How far can a bailee limit his liability by an express stipulation? In one of the cases the receipt stated that "all damage to perishable property is at the owner's risk." This was held to refer to loss resulting from the inherent qualities of the property stored. In another case the receipt stated that the "company will provide any desired temperature, but will not be responsible for results." This stipulation referred exclusively to the results of the temperature. In another case a bailee received cheese which was to be kept in a dry room at a specified temperature by means of overhead pipes filled with brine. The receipt stated that the property was to be kept at the owner's risk of loss from water. Nevertheless, the bailee was liable for damage caused by the dripping of water from the pipes resulting from the bailee's negligence.

Besides permanent structures erected for cold stor-

age, temporary cold storage may be effected in refrigerator cars. A carrier is not required to furnish such cars for carrying perishable property. But if a carrier receives butter, for example, for transportation, it must exercise care to protect it from the heat, and carry it in improved cars if such are in use; nor can the carrier escape liability for not safely transporting it on the ground that it did not have cars sufficient for that purpose.

Again, if a common carrier accepts fruit for transportation to a distant place, and, instead of packing it in a refrigerator car, packs it in a car through which cold air and snow enter, whereby the fruit is frozen, the carrier is liable for the damage and cannot shield himself behind a bill of lading exempting him from liability for loss caused by the weather.[1]

[1] See note on Cold Storage, 90 Am. St. Rep., 295-302. "If eggs are placed in a refrigerator car properly iced to prevent from freezing, and on arriving safely at their destination are placed by the carrier in its warehouse, it is still bound to use common and ordinary prudence in storing them, and if the warehouse is not a proper place for such storage in the winter time, the carrier is guilty of negligence and liable in damages if the eggs become frozen while in such warehouse." Ibid, p. 302.

CHAPTER XXVII

TRUSTEES

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3. Administrator defined.
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1. The term trustee includes a great variety of persons who act for others. The cashier of a bank, or director of a railroad is often called an agent or trustee, but we propose to include in this chapter executors and administrators, and persons technically known as trustees, who thus serve in discharging many well-known duties.

2. Let us begin by defining the duties of an executor. In another chapter we have explained the nature of a will, who may make one, how it must be construed; in short, all the leading features except the execution of the testator's wishes. He usually ap-

points one or more persons to execute his will; and their function or purpose is to settle his estate; in other words, to execute his directions in the manner set forth in his will.

3. An administrator is a person appointed by a court, existing for that purpose, to administer or settle the estate of a person who has died intestate, or without leaving a will or direction for the settlement of his estate. The duties of an executor and an administrator, therefore, in many respects are quite similar, and for that reason are often considered together in legal works, and accordingly we shall thus treat of them in this chapter.

4. A testator can appoint almost anyone to be his executor; his wife, one or more of his children, some friend; in short, almost any person legally capable of doing business.

(*a*) A minor is hardly a fit person though he is sometimes chosen;[1] and if a testator should appoint a person who, at the outset of his duties was mentally incapable of performing them, the court would set him aside and appoint another in his stead. The supposition clearly would be that the testator intended to appoint a person who was capable of administering the trust, and for every reason a person who should become incapable after his selection ought to be set aside, otherwise great harm might be done to every interest.

(*b*) Very often a testator appoints two or more persons as executors; this is a common practice. One object of doing so is to secure a more efficient admin-

[1] Wœrner's Am. Law of Administration, § 182, p. 433.

istration of the estate, as each is supposed to contribute something in the way of ability or experience. Nevertheless, when co-executors are thus appointed, they may act in many regards separately. As we shall soon see, the rule is quite different from that which applies to technical trustees. An executor, for example, can sign a receipt or draw money from a bank on his single check as executor; while both trustees are required to sign such an instrument to make it effective.

(*c*) Formerly, only individuals could act as executors, administrators, or trustees, but corporations are now specially authorised to act as executors, administrators, guardians, and trustees, for almost every kind of trust known to society. The most important advantage gained in appointing a corporation is responsibility. Nothing is more common than to hear of the abuse by an executor or administrator of his trust. Either through ignorance or fraud, or both, he squanders or loses the estate committed to his care. Corporations possess abundant means to respond to any mistake or negligence of which they may be guilty; and this advantage over that possessed by individuals is so great that the practice, especially among the possessors of large fortunes, is rapidly growing to appoint corporations as executors or trustees.

5. In appointing an administrator the statutes generally establish the rule. The next of kin is entitled to administer, and his relationship is ascertained in most states by the civil law; in others, by

the common law. Illegitimate and adopted children have no right to administer, unless the right is given them by statute. Among grandchildren, equally near the deceased, the following rules of preference are usually followed by the courts and also by some of the states: Sole administration is preferred to joint, male to female, unmarried woman to married woman, resident to non-resident, one most interested in the estate is preferred to one having the least interest or none.

In some states the law provides for a public administrator, who shall serve whenever there is no next of kin or near representative of the deceased. In other cases creditors have the right of signifying their choice. If the estate is likely to be insolvent and its efficient administration is important to the interests of the creditors, the selection of the administrator is of the highest moment and great care should be exercised in making the appointment. In many cases the statute is literally followed, and in the case of the death of a wife her husband is appointed, or vice versa, or the children of the father, and so on without any dispute or question.

6. Sometimes a testator omits to name an executor, or perhaps he may die before the testator himself. When this happens the court will appoint one or two executors, as the case may be, who are endowed with the same authority after their appointment as if they had been appointed by the testator himself. They are called administrators with the will annexed.

7. An administrator is required by law to give a

bond for the faithful performance of his duty.[1] This bond is signed by himself and one or two other persons or by a company as security. The purport of such a bond is, if he fails to administer his trust as the law prescribes, then he and his bondsmen are liable for the consequences.

A testator sometimes directs in his will that his executor need not give a bond; even when he is thus relieved, the court having jurisdiction of the settlement of his estate sometimes requires a small bond to be given. In the larger number of states executors are required to give bonds the same as administrators, and the amount in both cases is determined by the probable amount of the personal property.

8. Very often a person dies leaving both real and personal estate. If he is solvent the real property vests immediately in the heir, or heirs at law, and the executor or administrator has nothing to do with it except perhaps to lease it and collect the income. The title to personal property vests in the administrator, for the purpose of claims and distribution. He therefore takes possession at once, or if unable to do so he can bring a suit for this purpose. His right thereto is absolute and therefore his right of action is complete. He may bring replevin to recover the

[1] "In Florida, Georgia, Louisiana, New York, North Carolina, Pennsylvania and South Carolina executors are permitted to administer on the estates of their testators without giving an administration bond. In other states no distinction is made in the matter of requiring bonds between administrators and executors, unless the testator expressly direct, by provision in the will, that the executors by him appointed shall not be required to give bond, unless the court, upon complaint of some creditor, legatee or other person interested, or even upon its own knowledge, suspect that the estate would be fraudulently administered or wasted." 1 Woerner's Am. Law of Adm., § 250, p. 570.

property itself, or an action of trover for its value, or any other action, as if he were in every sense the absolute owner.

9. While the real estate at common law descends to the heirs or devisees, in some states this principle is changed by statute and the executor or administrator is given control during the settlement of the estate, or for such a time as may be needful to insure the payment of its debts. When he is satisfied of the existence of sufficient personal property to pay its indebtedness without resort to the real estate, then he may surrender it with due safety to himself and to the creditors.

10. There are some very difficult questions touching the property that he can, or must, take and hold for the proper administration of his trust. All personal property, of course, is vested in him, but there is a large amount of property, mortgages, and the like concerning which different rules exist. In general, a mortgage is an asset of the estate and goes to the executors or administrators; and the same thing may be said of animals, and the natural products of the land.

11. What shall be said of gifts that have been made by a testator or intestate? There are two kinds: inter vivos and causa mortis gifts. The latter kind does not become absolute; it is a peculiar kind of property.

12. A gift of this kind is invalid if needed to pay the debts of the donor, but if the estate is solvent, even then a question may arise between the donee

and the executor or the administrator. He may question the validity of the gift on the ground that the act of the donor was not sufficient to constitute a valid gift. The general principle is that such a gift to be valid must be in contemplation of death, and the money or other property must have been delivered. Consequently, if there has been no delivery, the gift fails. Perhaps the largest number of gifts coming within judicial view have been made by the depositors of savings banks.

13. There is less difficulty in determining whether an inter vivos gift is valid, because there is a delivery of the thing without condition or revocation. If the gift exists at all it is complete at the time of the delivery of the thing given.

14. A donor may make a gift and still be a trustee of the property, or the gift during his lifetime. Thus, a depositor in a savings bank may make a disposition in trust for another and exercise all the duties of a trustee in the management of the property. In the case of an ordinary out-and-out gift there must be a delivery and an acceptance, but when one acts as a trustee he retains possession of the thing given. Formerly, it was said that a beneficiary must be notified about the gift, but this seems to be no longer requisite in order to make a valid donation. When the beneficiary is informed it is simply another link in the chain of evidence.

15. In many cases trusts are created, not with the intention of making an actual gift to anyone, but simply of evading some law. Thus, some of the

states provide that a savings-bank depositor must be restricted in his deposits to one or two thousand dollars, and in order to evade the law he deposits the money in trust in the name of A, B, and C. As the trust is created simply to evade the law, and not to make a valid gift for the benefit of the persons named, the courts do not hesitate to declare the gift to be invalid.

16. An executor or administrator must proceed at once to recover property that has been conveyed by the deceased for the purpose of defrauding his creditors, for in administering an estate all just debts, if possible, must be paid. These must be liquidated or discharged before legacies or other sums can be paid to the heirs except in the case of a few priorities, like the priority of a wife to share in the estate of her husband. The law regards her not as a preferred creditor, but as having an estate which cannot be taken away without her consent.

17. On the death of the testator, or intestate, the first duty of the executor or administrator is to make an inventory of the estate. The object of this is to find out the amount of his trust, both for his own enlightenment and for that of the court. This inventory is made by the administrator with the assistance of two or three persons called appraisers. This proceeding is not required in every state, but in most of them. Obviously, the first step in executing an estate is to know the kind of property, its worth and characteristics.

18. Having done this, the next step is to notify

all creditors to present their claims, which must be done within a period prescribed by law. This is not very long, usually about six months, which experience has shown to be quite long enough. It does not follow that the exact amount of the claim must be settled within this period, but simply that notice of it must be given, or it will be cut off. If an estate be large and complicated there may be many disputed claims that can be settled only by judicial ascertainment. Thus, years may pass before the exact amount of the indebtedness of the deceased is fully ascertained.

19. On the death of a person, if it is known or believed that his indebtedness exceeds the amount of his property, the administrator requests the court to declare the estate insolvent, whereupon he proceeds to settle it as an insolvent estate. Sometimes he begins his work believing there is ample property to pay all claims, besides a large balance for distribution, and is greatly surprised by the presentation of unexpected claims, which, if valid, will render the estate insolvent. He then makes an application to have the estate declared insolvent and proceeds accordingly.

20. The mode of dealing with an insolvent estate is quite different in several ways from the mode of dealing with the other. In a solvent estate the administrator in some states has a wide latitude to determine the worth or validity of every claim; in other states his authority is restricted. It will be readily seen that this is a great authority to commit to an administrator, and may be abused. An unfit or incompetent administrator, or one who was bent on defrauding

the estate might take advantage of his position to disallow claims; in short, to commit great wrongs.

21. For this reason some states have virtually entrusted the authority to decide the worth of claims to a court or commission. In such states an administrator's authority to deal with claims is nearly or entirely gone.

22. While creditors are presenting their claims the administrator is collecting the assets belonging to the estate. Not infrequently he is obliged to sue debtors; and several months pass before he is in a condition to pay the creditors anything. Sooner or later he succeeds in collecting the assets, and the commissioners in ascertaining the liabilities. The next step is, by virtue of an order of court, to make a dividend or allowance to creditors. Sometimes several dividends are made, the first after collecting a portion of the assets, and the second after collecting still more, and so on until all the assets have been collected and divided.

Occasionally an insolvent estate proves to be solvent, and of course all the creditors are paid in full, and the balance, if there be any remaining, is distributed as the law directs.

23. If the real estate is needed to pay the debts of the deceased, it may be taken for this purpose. It will be seen, therefore, that the heir, or devisee, who has the title and may be in possession, is not quite the absolute owner until this question is determined. If it is not needed then the title of the heir is complete in every respect, and he is as fully entitled to

the possession and income as any other property he may own or possess.

24. As the expense of administering an insolvent estate is somewhat greater than that of administering a solvent one, it is preferable to carry the estate through as solvent if this can be done. On the other hand, if it is apparent at the beginning, or at any time afterward, that it is insolvent the only course is to have its insolvency declared and to settle it accordingly.

25. In collecting the assets of the estate it may be needful for him to make a temporary investment for the purpose of adding something to the amount. He may deposit the money in a bank, and if he did so, exercising proper judgment in the selection of an institution, which afterward failed, he would not be personally responsible. He ought to receive some interest, if possible, from the temporary use of money, but in no case is he justified in retaining this as a perquisite. All the income derived from the assets of the estate, either directly or indirectly, should be added thereto. From this rule there is no exception.

26. In selling personal property he may act on his sole authority, unless governed by the statute provided for such cases. Very often he is required to make an application to the court for the sale of property belonging to the estate. Certainly this is much the safer course for him to pursue.

Sometimes the deceased was a member of a partnership, and it is very important, perhaps, to continue the business for a time at least before withdrawing

the money he had invested in the enterprise. It may be, if the money were suddenly withdrawn, serious harm would result to the surviving partners, or perhaps the full amount could not be obtained belonging to the deceased. At all events the interests of both parties are often best served by continuing for a time the business. In such cases an executor or administrator may possibly have to take a large personal risk himself, as the court may have no authority to permit him to act temporarily as partner in place of the testator or intestate. In some states experience has shown the need of endowing an administrator or an executor with authority to act thus for a short period, and power has been given him accordingly. Whenever it does not exist he acts wholly on his own responsibility. When thus acting it is certainly his most prudent course to inform the court, and if it cannot shield him in any manner, his notification will tend to show his good intention, at least, in thus continuing to act temporarily as substituted partner.

27. Finally, after collecting the assets, paying the bills, and dividing partly or wholly the estate, errors may be discovered, or still worse, frauds. In such cases the estate may be opened for further action. It is a familiar principle of law that a statute of limitations does not run against a fraud. In other words, whenever a fraud has been discovered in the settlement of an estate, or in the execution of any trust, the persons interested have a specified period of time, several years at least, after their discovery, to

take action against the wrong-doers. Should the persons thus interested neglect, however, to take action within the period prescribed, then the fault would be their own and their remedy would be cut off. It therefore happens that estates are opened either for one or both of these reasons years after final settlement, but when at last a settlement is reached then the statute of limitations becomes operative to bind all the parties interested; and after the statute has run for the period appointed the estate or trust is closed and all possibility of future action is ended.

28. In a testate estate the testator himself has directed the mode of distribution. But it must not be forgotten that in no case can he distribute his estate to the prejudice or injury of his creditors. They have the first claim to the property and must be first paid in all cases of doubt or uncertainty. Of course, if there is no doubt whatever concerning its solvency, the executor may proceed at once to pay the legacies, and to part with the real estate.

29. Having now treated in a general way of the duties of an administrator and executor, let us consider the duties of a technical trustee. Very often a person provides in his will that a specific sum of money shall be given to his children in trust. By this he intends that the property itself shall go into the possession of one or more persons as trustees who are to pay over the income to the persons designated, during a given period, or during their lives. Very often he leaves young children, and provides that all of his property given to them shall be kept

in the possession and control of the trustee until they respectively reach the age of twenty-one, at which time he shall deliver to each one his respective share. Meanwhile, the trustee is to pay to each of them, at perhaps stated periods—monthly, quarterly or otherwise—the income accruing from the property.

30. Formerly trusts were much more complicated in form, and property was often tied up during the lives of several persons. The law in this country has rather frowned on such dispositions. By statute in many states the right to create trusts for long periods of time and for many lives has been abolished. Yet everywhere the right to create trusts exists, and they fulfil a most important function. In every state they are numerous, and are executed either by individuals, or by companies created for that purpose.

31. An executor may be a trustee. The two offices rarely conflict with each other. For example, a testator may also direct that his executor shall act as trustee for A, in addition to performing his duties as executor. Sooner or later the property he holds at first as executor is subsequently retained by him as trustee, and his duty as executor is ended.

32. A trustee should not be a minor. He should give a bond in order to secure his beneficiary, the same as an administrator or an executor. He should also file an invetory of the trust property for the benefit of all concerned.

33. A trust will not fail simply because there is no trustee, because the court is competent to appoint one should the trustee or trustees designated by the

testator die or become incapable of acting. Sometimes the court will appoint a temporary trustee, though this is unusual.

34. Sometimes a person intermeddles with trust property without legal right. He is called a trustee in his own wrong, and is liable for so doing.

35. The duties of a trustee are varied. The testator rarely prescribes only the most general terms for his guidance—to preserve the estate committed to his charge, and to pay over the income and principal in the manner directed. But he has obvious duties to perform while the property is in his custody and control.

36. In executing these he may render himself liable for negligence in many ways.

(*a*) For example, it is his duty to have the trust property properly assessed, just as other individuals must have theirs; and should he neglect to perform this duty he would be personally liable for the penalty visited on transgressors. He could not, after paying the penalty, add the sum as a charge to the estate.

(*b*) He is also liable for the negligent use of the property. If it consists of a house it is his duty to keep it in proper repair, and should a person be injured by snow from the roof, or from his negligence to repair the sidewalk, or from the negligent overflow of water, he would be liable personally for the consequences, just as an individual under similar circumstances.

(*c*) The law prescribes rigidly that a trustee cannot

use the estate for his own personal benefit. In no case can he sell it to himself. The law jealously guards against this temptation by declaring that all attempts to transfer it to himself as owner are futile and illegal.

(*d*) For the same reason he cannot pledge the trust estate as security for his own debt. He cannot speculate with the funds committed to him, however honest may be his intention. He should not deposit them in a bank to his own personal credit, though this is often done, whereby they become mixed and lost to the beneficiaries.

37. Sometimes a trustee fails and makes an assignment; this does not include the trust property. It remains as before, distinct from his own, and cannot be taken for his own individual indebtedness.

38. The trust property may be taken for any indebtedness growing out of the execution of the trust within its legitimate scope. Of course, the trust-maker may limit in various ways the execution of the trust, and these limitations may be so effective in the way of notice to creditors as to cut them off from recovering anything made on contract with the trustee in plain violation of his authority. Unless limitations are thus imposed, a trustee may make lawful contracts pertaining to the execution of the trust, and subject the estate or income within his dominion for payment.

In like manner a mechanic's lien cannot be laid on a trust estate, except in those cases wherein the trustee has power to contract for the labour or the materials

furnished. The trust itself usually is a proper guide to all contractors or creditors, and they must govern themselves accordingly.

39. On the death of one of several trustees, both the office and the title to the estate vests by survivorship in his co-trustee; when a sole trustee dies, either by statute or by common law the property vests in his successor in trust, and in that manner the trust continues as before.

40. The general powers incidental to the office comprise those that are necessary for performing his duties, the power to administer, receive, and sue for the trust property, or any income accruing thereto, to invest the funds and lease the real estate, to keep it repaired and insured, to disburse and distribute the property, to protect the beneficiary, or maintain him if incapable of maintaining himself.

41. Authority to sell the trust property, and convert real into personal estate and vice versa, are usually bestowed on a trustee by a legislature or court. It is special, and not general, and incidental to that office, since the original conception of a trustee was a person entrusted with the title to the property, and not a business manager.

42. The execution by two or more trustees of their power is joint, and the execution even by a majority is void, unless the will or other instrument creating the trust authorises such action. Consequently the insanity or refusal of one trustee to serve may block all action; and the only remedy is the removal of one or more and the appointment of others in their place.

This is a delicate function for the court to perform, and will not be undertaken unless the conduct of a trustee is factious, unreasonable, or corrupt.

It is true that in many cases one or two or more may do many things that will bind all. Thus, one trustee may collect dividends, rents, interest or any income, receive a simple debt or discharge a mortgage, but he cannot assign or sell a mortgage, collect a judgment, or bind all by a compromise.

43. The power of a trustee is personal and cannot be delegated, either to a stranger, or by one trustee to another. It is the very essence of trusteeship that the person appointed shall act.

It is also true that many matters may be confided by a trustee to another who merely acts as the instrument or agent of the trustee himself. Thus, a trustee, who employs another to collect rents, is regarded by the law as collecting the rents himself. The distinction, although narrow, is pretty clear between the cases in which a person is employed as an instrument of the trustee in carrying out his direction, and the cases in which the employee is exercising a discretionary power himself. A trustee might very properly employ a lawyer to make out a conveyance of trust property; it would be quite another thing to ask the attorney to sell the property; for the latter act is solely within the boundaries of the trustee's power and cannot be confided to another.

44. Another important matter is the power of sale committed to a trustee. In many states the statutes prescribe the authority of trustees in this regard.

(*a*) Let us consider the subject of real estate first. Not infrequently it is desirable to sell in the interest of his beneficiary. In most cases the trustee cannot do this on his sole judgment; and must apply to the proper court for authority to sell. It may be that, by virtue of the power creating him a trustee, he can sell the real estate and invest the proceeds in other property; more often than otherwise he must act through the intervention of the proper legal tribunal.

(*b*) It is his duty, so long as he is in possession, to lease the property and on the best terms obtainable. He has a wide latitude in making terms with a lessee. It is sometimes said that he cannot make a lease beyond the period of twenty years; in many states no limitation of time exists.

(*c*) He must keep the property insured and in adequate repair; in short, must exercise his authority for the best interests of the beneficiary. Should he neglect to improve it properly, or prevent its deterioration, or fail to lease it without good reason, such negligence would be just cause for complaint, and ultimately for his removal. For it must be remembered that the creator of the trust has always in mind the welfare of the beneficiary, and expects that the trustee will fulfil his duty efficiently and honestly.

(*d*) A somewhat different rule applies to the management of personal property. Besides attending to its safety, he must obtain, if practicable, a proper income therefrom. If, therefore, the property is invested in bonds bearing a very low rate of interest, and other bonds can be obtained, quite as safe and bearing a

higher rate, it would be the trustee's duty to make an exchange, in order to enhance the beneficiary's income.

(*e*) The statutes in many states describe the kind of securities in which a trustee may invest; these release him from a serious burden, because, so long as his investments are within the prescribed limits, no one can justly complain.

(*f*) In selling personal property he has a wider latitude of acting without the intervention of the court, but in some of the states he is also required to make application as in the case of the sale of real estate.

(*g*) After selling the property he must put the money safely in bank and seek to secure an income therefrom while awaiting reinvestment. A trustee would not be justified in keeping the money thus derived from the sale of trust property long in idleness unless an extraordinary condition of things existed. One can imagine that, during a declining market, a trustee might hesitate to invest until he felt assured that the bottom had been reached; but, ordinarily, he must use all proper diligence consistent with safety to obtain a reasonable income from the trust property.

45. A trustee has no power to pledge or mortgage the trust property, even though he has authority to sell and dispose of it. This rule is disputed by some authorities, who maintain that the greater power includes the lesser; yet this is not the better rule.

46. A trustee has authority to bring and to defend suits for the protection of trust property. To that

end he can employ counsel and incur all necessary expenses needful to preserve the trust fund.

47. It is the duty of a trustee to maintain and support his beneficiary. How far he can go in this direction often depends on the instrument creating the trust. Not infrequently this declares that only the income shall be paid to the beneficiary; in such a case the duty of the trustee is clearly limited. In other cases he has authority to go further and to sell, if need be, the trust property or a portion, from time to time, and devote the avails in the same manner.

48. If he would neglect or decline to carry out the provisions of the trust, in accordance with the maker's intentions, this would be good cause for removing him from office. To a large degree his duty is discretionary, and when this exists a court will not interfere, save in a clear case of failure on his part to exercise his discretion reasonably.

49. In some states he is entitled to no compensation for his services; in most of them he may be reasonably paid. The amount is measured by the difficulty and responsibility of the service.

CHAPTER XXVIII

CORPORATIONS

§ 1. Stockholders

1. Who can form a corporation.
2. Can another corporation become a stockholder?
3. Consideration for shareholder's contract.
4. Right of withdrawal.
5. Agreement to subscribe for shares in a future corporation.
6. When contract becomes binding.
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1. Who can form a corporation? Generally it may be composed of all persons who are able to act in their individual capacity. Once it was questioned whether a married woman could be a subscriber for shares, because of her incapacity to make a contract; even now, in forming a national bank, the usual practice is, whenever she wishes to become a stockholder to act through some friend, or her husband, if she has sufficient confidence in him. After completing the organisation then the shares are transferred to her name and thereafter she becomes liable like any other stockholder.

For the same reason a guardian can hardly act as an original subscriber for shares because of his disability or incapacity to act either for himself or for his ward in some matters in the early stages of organising.

2. A more important question has arisen concerning the rights of other corporations to become original subscribers. This is largely regulated by statute. A national bank is forbidden from becoming a subscriber to the stock of any bank or corporation, and the same rule applies to many other corporate associations. On the other hand, modern business has so changed that it is often desirable for corporations to become original subscribers.

3. A question once existed concerning the consideration for the contract of subscription. The modern doctrine is that a person is bound by his subscription because the statute makes the obligation imperative.

4. Whether a person can withdraw before the subscriptions are complete is still perhaps an open ques-

tion. The more general view is, he has a right to withdraw until the subscription is rendered complete by enough subscribing to fulfil the law. When this is done then all are bound by the undertaking.

5. Whether an agreement to subscribe for shares in a future corporation is equally binding is another question. In that case there is no offer which a corporation can accept, and the parties do not become stockholders and cannot be thus charged unless they subsequently carry out their agreement by subscribing for the shares. An offer to become a stockholder in a future corporation may undoubtedly be revoked at any time before acceptance.

6. An offer or contract to become a shareholder does not become binding until all conditions on which the offer or contract was made have been performed. No liability is incurred unless the corporation finally organised is the one contemplated at the time of the agreement.[1]

7. Unless the statute prescribes otherwise, the contract of membership may be formed by a voluntary association of the members. Their intention to assume such relationship to each other is the only essential thing. Thus, the intention of individuals, to whom a charter has been granted unconditionally, to form themselves into a corporation may be shown by the simple acceptance of the charter. The same rule applies to an amended charter or subscription; no special form is required to give validity to the intention of the parties unless the law requires this to be done. Gen-

[1] For form of agreement to sell shares see Vol. VI, Appendix, No. 24.

erally, the corporation laws and charter describe in detail the methods of forming corporations, and of course these must then be pursued.

8. A statutory subscription for shares is something more than a mere offer to take and pay for them.

(*a*) It is like the liability of a banker to contribute his shares of capital fixed by the articles of agreement. The contract of the shareholders is not mutual like that between the members of an unincorporated association. The contract is complete as soon as all the preceding conditions prescribed by law have been fulfilled. The stockholders then become entitled to all the rights and privileges; may vote at corporate meetings; claim a share in the profits of their common venture; become liable for all the obligations of stockholders; and must contribute the capital subscribed by them to the enterprise.

(*b*) The contract between statutory subscribers depends for its validity on the statute under which it is formed, and not merely on the common law. The intention of the legislature therefore in providing for the opening of stock books is to make a subscription binding from the time it was made. Otherwise the greatest facility would be given for practising frauds on innocent subscribers by means of subscriptions intended merely as a decoy. A subscription for shares made after the organisation of the corporation does not become binding until it has been accepted by the company through its proper agents.

9. Sometimes fictitious subscriptions are made to induce other persons to subscribe. There is a secret

understanding perhaps that no liability shall attach to the subscribers or that they shall be allowed to withdraw whenever they please. On the discovery of the fraud the subscriber who has been defrauded can do one of several things. If he has paid his money he can bring an action to recover it. If he has not paid, and is sued for the amount, he can repudiate the contract, and set up the fraud as a defence. He still has a third remedy—to accept his stock and sue for the damages sustained by the deceit that has been practised upon him.

Should the company become insolvent he is thereby prevented from rescinding his contract and recovering fully for the injury he has sustained. In such a case he may pursue the agent or party who by his fraudulent representation induced him to subscribe for the stock. A few years since there was a noteworthy case in Scotland in which the directors were held guilty for thus persuading persons to subscribe, and were made to pay heavily for the consequences of their misdeed.

When persons have thus subscribed who are not in one sense genuine or true subscribers, the bona fide ones cannot use these facts to release them for their own subscriptions. In other words, the existence of a fictitious subscriber in a body of stockholders does not, on the discovery of the fact release the bona fide ones from their undertaking.

10. Sometimes shares in excess of the amount allowed by the charter are subscribed after the formation of the corporation. The subscriptions taken beyond the full amount are void and the subscribers are

not members of the corporation. Sometimes the law provides for the allotment of shares among all the subscribers when the amount is not sufficient to supply all the subscribers. In such a case the contract between the subscribers remains incomplete until after making the allotment.

11. A subscription may be made to depend on performing preceding conditions. A subscriber does not then become a shareholder until the conditions have been performed. Until then he does not become entitled to the privileges, nor subject to the liabilities attaching to the status of a shareholder.

12. Subscriptions that are conditional on the happening of a future event must not be confounded with subscriptions made subject to special terms. In the former case the subscribers do not become stockholders until the prescribed condition has been fulfilled. In the other case after the event has happened they become shareholders on the same terms as other members.

13. The issuing of a share certificate is not an essential condition of ownership. It is merely evidence of ownership, and may be demanded by virtue of one's right of membership.[1]

14. The issue of new shares by a corporation may be by ordinary subscription or by sale. (*a*) There is an important difference between the two methods. A person who agrees to purchase shares intends to buy the certificates as salable securities. Delivery of them, therefore, and payment are intended to be concurrent acts, and on the failure to carry out the contract

[1] For form of certificate see Vol. VI, Appendix, No. 23.

neither party can charge the other, without averring a tender of performance. On the other hand, the effect of an original subscription is to make the subscriber a shareholder at once, with a right to vote at meetings and liability to share in deficiencies and for assessments. The delivery of a certificate of shares is never a condition precedent to the liability of a shareholder for a contribution after a proper call has been made.

(*b*) Whenever the capital stock of a company is increased under a power conferred by its charter, each stockholder has a right to a proportionate number of the new shares before they can be offered or issued to strangers. Unless he waives this right, he may maintain an action against the company, should it deprive him of them, for the loss he has sustained. The measure of damages is an excess of the current value of stock above the par value at the time of payment of the last installment with interest on the excess.

15. Preferred stock is sometimes issued, and is so called because the owners possess more rights than other stockholders. Generally, preferred stockholders have a right to receive dividends from the earnings of the company before the holders of the common stock can share in them.

(*a*) Usually, such stock is issued to raise money for corporate purposes instead of borrowing on bond and mortgage.

(*b*) A preferred stockholder in some respects is like the others, only he is entitled to a preference over them in distributing the profits. Such dividends are

payable only out of the net earnings. Even a guaranty of dividends on preferred stock is not an absolute obligation; only a promise to pay the dividends that are earned.

(*c*) The owners of preferred stock generally, though not always, have the right to vote at any meeting of the holders of the capital stock. In issuing certificates to them it is stipulated whether they have the right to vote or not.

(*d*) Preferred stock may be so issued as to make the transaction strictly a borrowing; and the stockholders creditors. They are not liable for the debts of the corporation.

16. Whether a contract with a corporation is to purchase shares, or to become a present member, depends on the intention of the parties. When the payment of the price and delivery of the certificates are intended to be concurrent acts, the transaction will be a purchase and sale; when the contracting party is to have the rights of a shareholder before the whole amount of shares has been paid, the contract is one of membership.

17. A contract of membership like any other cannot be created without the mutual consent of the parties. Consequently were a person's name put on the subscription books without his authority, the subscription would not bind him. Nor does a person who subscribed through a pretended agent, who did not possess proper authority, become a shareholder. The unauthorised subscriber can subject the subscriber to an action for damages.

18. Again, an alteration in the articles or an attempt to transfer the subscriptions to a new company will release a subscriber unless he has consented to the change by some word or act indicating his acquiescence.

19. The power conferred on a board of directors of allotting shares to applicants cannot be delegated to a committee composed of a part of their number. No valid allotment therefore can be made except by the board.

20. An irregular subscription made before the complete corporation may be treated as an open offer and accepted by the corporation after the organisation has become complete.

21. The directors usually have authority to dispose of unsubscribed shares. Whether they are bound to observe the same conditions as limit the powers of commissioners before organising in receiving subscriptions depends on the charter or statute. The general rule is they are not thus limited unless the contrary appears.

22. The authority of agents or commissioners to receive subscriptions is strictly limited to the duties they are required to perform. They cannot refuse to receive a subscription made by a competent person, nor release a subscriber, nor accept subscriptions on special conditions. A person who acts as agent for another without authority may have the defect cured generally by subsequent ratification.

23. A failure to comply with the forms prescribed by law in entering into a contract of membership does not prevent a person from becoming a de facto share-

holder. The authority of original agents to receive subscriptions is undoubtedly limited by prescribed conditions, and an irregular contract would be contrary to law. This want of authority may be cured by a later act of incorporation. The mutual relationship existing between shareholders and the equitable rights of creditors must be considered.

24. A subscription for shares is a contract in writing and cannot be proved by parol evidence unless the original subscription paper is lost and proof of this has been given. Furthermore, the terms of the contract cannot be varied by parol evidence of a special agreement made prior to, or at the same time with the subscriptions.

25. A contract is not rendered voidable unless it represents facts which the defrauded party was under no obligation to learn for himself.

(*a*) A person who makes a contract must, at his peril, inform himself concerning the legal consequences of the undertaking. A simple misunderstanding about its legal effect is not sufficient ground for avoiding it. If this were not the rule mutual dealings would be impossible. A subscriber for shares must ascertain the contents of the subscription paper which he signs, the provisions of the charter of the company, and the general laws that affect it. A fraudulent representation, therefore, relating to these matters, or to the rules and duties regulating their membership in a company, does not give the subscriber the right to avoid his contract.

(*b*) A fraudulent representation about the actual

contents of a subscription paper or articles of association, without negligence on the subscriber's part, may be a good ground for avoiding the contract. Thus, a person who was unable to read and did not know the contents of the paper and who was induced to become a shareholder by a false representation concerning its contents, was relieved.

A contract is voidable for a fraudulent representation of facts, but not for a breach of agreement by either of the contracting parties. Therefore a failure on the part of a corporation to comply with the special terms of a subscriber does not render the contract voidable, but is merely a cause for action against the company.

(*c*) Subscriptions obtained by an agent by means of false and fraudulent statements concerning the happening of a future event, or the doing of a future act, cannot as a rule be avoided. Thus, a statement made by an agent that a proposed railroad would be built on a certain route within a fixed period of time would not render a subscription secured on the faith of it voidable, though he intended to deceive, and in truth does deceive, whenever the road is not built as promised.

(*d*) Whether a shareholder's contract be voidable for false representation must necessarily depend on all the facts that surround the transaction. Morawetz says, as a general rule any fraudulent representation with regard to the financial state of a company or its arrangements for carrying out its enterprise, or with regard to any other fact which can reasonably be sup-

posed to have been material in inducing a person to become a shareholder will enable the latter to avoid his contract. If a person is induced to take shares by false representation that another person has become a shareholder, or that certain persons have agreed to act as directors of the company, this will be a ground for avoiding the subscription, but it must appear in such case that a subscriber relied upon the statement and was induced thereby to take the shares.

(*e*) A person who has been induced by fraudulent statements to become a subscriber must proceed quickly to annul his contract, provided he desires or intends not to be bound thereby. On one of these occasions Lord Romilly said that a man must not play fast and loose. He must not say, "I will abide by a company if successful, and I will leave a company if it fails"; therefore, it is the subscriber's duty to determine at once whether he will depart from the company or remain a member.

26. Sometimes shares are cancelled. A certificate of shares is merely evidence of the shareholder's ownership, and consequently its cancellation does not relieve him from membership in the company. On the other hand, a certificate issued illegally or to a wrong person does not make him a holder, and its cancellation would merely destroy an invalid instrument.

27. The purchase by a company of its own shares is in effect to withdraw them and reduce its assets. This cannot be done unless the law specially provides for such action. Every continuing shareholder is injured by a reduction of the fund, and the creditors

who have trusted on the consideration of the capital originally supplied have a reason for complaining. A reduction therefore, whatever form it may take, must be done in an open manner as the law prescribes. But if a company (having no indebtedness at a given time) should thereafter reduce its capital and then contract a new indebtedness, it would furnish no ground for complaint on the part of the creditors, unless, perchance, the reduction of the capital was done in such a secret manner as to operate practically as a fraud on them.

28. At common law a corporation has no lien on its stock for the owner's indebtedness, but in many states a lien has been imposed by specific statute or charter. And wherever the right exists the lien is not destroyed by violating the law restricting the amount that may be loaned to a borrower, except for the excess. In no case can the lien operate retrospectively.

Once, a corporation could establish a lien by usage; or by by-law under the general authority given to a corporation to regulate the mode of transferring its stock. While in some states this is still the law, the current of judicial decision is running so strongly against secret liens that the right to fasten a lien on stock by by-laws is denied unless the authority is clearly conferred by statute. This tendency is doubtless strengthened by the federal prohibition against the creation by a national bank of any lien on its stock. But a bank is not prevented from retaining a dividend that has been declared to lessen or discharge the indebtedness of the owner to the bank; for the money

thus due to him is like any other free money he may have in the bank's possession.

Again, the directors of a corporation may receive its shares in the way of gift, bequest or payment in satisfaction of its debts. The law seeks to guard every company against losses by its debtors, and to this end provides that a company may take its own stock to avoid a loss. It is true that to this extent the fund that may be used for paying creditors is lessened. To obviate all danger of loss to them the law usually provides that the stock thus taken must be sold again within a stated period in order to preserve the amount of the company's capital. More properly speaking, the shares thus received are extinguished and new ones are created to fill their place. By a fiction, says Morawetz, these new shares are considered as if in all respects they were the old shares, and the corporation merely an immediate transferrer, but it would be an absurdity to say that a corporation can really hold shares in itself.

29. The members of the corporation may be compelled to pay for their shares by an action brought in the company's name. But it has no lien on them to secure the payment of assessments unless its authority is conferred by statute. Nor can the shares be forfeited and sold for the non-payment of assessments except by express authority.

30. A shareholder on whom calls have been made cannot defend by saying that the agents of the company have exceeded their authority and done unauthorised acts. Their failure to manage its business in

a legal manner is no defence in an action against him for not paying his share of the capital. In like manner directors cannot release some of the shareholders and cancel their shares. Acting without authority, the release would not bind the company, and would be wholly void.

Furthermore, a delay in completing the works of the company or in prosecuting its business will not discharge a stockholder from his obligation. Creditors are entitled to all the capital subscribers have paid, or have promised to pay, and ordinarily there is no escape from this obligation.

31. Some charters provide that the shares of stockholders may be declared forfeited and sold for the non-payment of assessments. This power must be construed strictly. A valid forfeiture can take place only by acting in a strictly legal manner. If the law prescribes a notice to be given to delinquent shareholders before forfeiture of their shares, this must be literally executed. If a sale by public auction is required a private sale would be void. Moreover, a sale for the non-payment of assessments would be void if this were unauthorised.

A grant of a power to declare a forfeiture does not exclude the common law remedy against the delinquent shareholder. The agents of the company may therefore proceed, either to collect the unpaid calls, or by way of forfeiture and sale of the delinquent member's shares.

A shareholder's liability ceases after the forfeiture is complete and his connection with the company is

severed. A charter that provides for the sale of the shares of a delinquent member presumes that he would retain his membership until the disposition of them, consequently his liability would continue until that time and he would have a corresponding right to redeem them.

He may therefore satisfy calls on his shares and prevent a forfeiture at any time before the proceedings are complete, and he has ceased it to be a member. But after the sale has taken place it is impossible to reinstate an owner and no right of redemption exists.

32. Lastly, the liability of shareholders is determined by charter or statute. The shareholders of national banks may be liable to creditors for an amount equal to the par value of their stock. For example, if a bank possessing a capital of $1,000,000 should fail, owing depositors $1,000,000 and the assets or funds remaining should amount to only 50 per cent. of this sum, the shareholders would be obliged to contribute $500,000 more to pay the creditors. One reason why corporations are formed is to limit the liabilities of shareholders; for, if they acted as partners, then each would be liable for all the debts of the concern. In a general sense, all the shareholders are partners, interested in the common business, sharing its profits and losses, but with a limited liability. Every shareholder knows in the beginning that he cannot be rendered liable above the amount prescribed by law. This is one of the chief reasons for the rapid growth of corporate business institutions.

33. A corporation consists of the whole number of

its members. It cannot. therefore, carry on business without the aid of agents, for the unanimous action of the stockholders would otherwise be essential to every act. There is an implied condition, therefore, in forming a corporation that the majority of members present at a shareholder's meeting shall have authority to bind the whole association by their vote. The powers of the majority are increased by charter or statute. Says Judge Lindsay: each and every shareholder contracts that the will of the majority shall govern in all matters coming within the limit of the corporation.

§ 2. Kinds and Authority of Corporations

1. Kinds of corporations.
2. Corporation sole:
   - *a.*—Described,
   - *b.*—Why an individual thus styles himself,
   - *c.*—An individual may become sole owner,
   - *d.*—He may be liable as a corporation for its debts.
3. Corporations aggregate, and how they are classified.
4. Foreign corporations.
5. Ways of creating corporations; how a legislative character is obtained.
6. Creation of a corporation by complying with the requirements of a general law.
7. Duration of a corporation.
8. It lives through successors and not heirs.

9. Authority of a corporation is granted and continued by the state.
10. Its use of a seal.
11. Authority or privilege conferred on it is called a franchise.
12. Every corporation must have a name.
13. Corporation can sue and be sued.
14. Corporation can hold real estate.
15. Annual meeting.
16. Hour and place of meeting.
17. Power of majority.
18. Ratification of action of majority by all.
19. Meeting must be called in proper manner.
20. Remedy when officers refuse to call it.
21. Distinction between mode of calling regular and special meetings.
22. Adjournment of authorised meeting.
23. Members may adopt by-laws.
24. What by-laws can be adopted.
25. Every by-law must be reasonable.
26. Banking by-laws.
27. By-laws relating to savings-bank deposits.
28. Railroad by-laws.
29. By-law prescribing a lien on stock for debts.
30. By-laws do not affect non-members.
31. Shareholder only can vote.
32. Holder of record is the only rule.
33. Restriction on voting power.
34. Right of trustee to vote.
35. Joint owners.
36. Illegal votes.

37. When they will not be thrown away.
38. Voting by proxy.
39. Corporation cannot vote its own shares.
40. Appointment of inspector of election.
41. Corporation can do business in another state.
42. Opinion of United States Supreme Court.
43. Can do whatever is not prohibited, or contrary to state policy.
44. Rules of comity have the force of legal obligation.
45. Tax or license may be imposed.
46. Regulation of business of foreign corporation.
47. Suits.
48. Directors' meetings outside the state.

1. There are many kinds of corporations. The term *quasi* is applied to some of them, by which is meant associations or institutions that resemble corporations in some ways, but not in all. The supervisors of a county, the trustees of public schools and similar officers, are clothed with well-defined power. For example, the supervisors of a county can own and manage real estate for its use. These bodies can sue and be sued like other corporations, and are therefore thus regarded.

2. Another kind of corporation, called sole, is formed by a single person, a king or a queen.

(*a*) Such corporations are not very frequent in the United States, yet exist to some extent, especially in the church. A bishop is sometimes invested with the title and keeping of property given for church purposes, and is a corporation of this character.

(*b*) Although a single individual cannot form a corporation, not infrequently an individual, especially when engaged in banking, has styled himself a bank. Of course, his object is apparent—to gain the confidence of those who would not do business with him if they knew that he was acting solely for himself, without partners.

(*c*) The same rule does not apply to a person who purchases all the stock of a fully formed corporation. The corporation still survives. Thus, were a banker taxed by a state lower than a bank, the sole owner of a bank could hardly escape paying the higher rate on the ground that, after all, the corporation was not a bank but a banker. The law would say to him very plainly: So long as you preserve or continue this corporation it is thus recognised by the law, and you must pay the tax accordingly. The law regards the corporation as in abeyance awaiting a resurrection or restoration which may come at any time by the will of the owner.

(*d*) Though a person acquires sole control, he is liable in a corporate manner for the debts of the concern. This question was decided not long ago in Kentucky. By preserving the entity of the corporation, on its failure he was required to pay its debts in the same way and to the same extent as if the corporation itself in every sense of the word had failed.

3. Most of the corporations in this country are called corporations aggregate, and are divided into several classes. First, religious corporations that are organised for religious purposes. Secondly, corporations embrac-

ing all that are not religious, and are divided into eleemosynary or charitable and civil. Illustrations of eleemosynary or charitable corporations are religious academies, hospitals, and the like. Civil corporations are again divided into two classes—public and private. Public corporations are formed for governing, of which cities and towns are examples. They are often called municipal corporations, and are created by the legislature of the states wherein they exist. They possess no natural or original authority; only such as are given to them by positive law or legislation. Some have contended that a town is an original form of government, possessing all the inherent authority not taken away by the state or the federal government.[1] Though town governments in New England states are much older than city or county governments, yet they derive, like them, all their life and authority from a legislative source. Lastly, private corporations may be mentioned, which are founded for private purposes and are the most common. Insurance companies, railroads, banks and the like, are private corporations. To some extent they are public corporations, because they derive their authority from a public source, and because the legislature may make regulations concerning them. A railroad corporation, though classed as a private corporation, may be taken by the state, after payment, because it is created by the state and possesses

[1] "Associations and government institutions possessing only a portion of the attributes which distinguish ordinary private or public corporations have sometimes been denominated *quasi* corporations. Towns and other political divisions, school districts, boards of commissioners, overseers, or trustees of the poor, etc., having authority to act and bring suit as united bodies without regard to their membership for the time being are *quasi* corporations of a public character." 1 Morawetz on Private Corp., § 6, p. 6 (Second Edition).

a public character. If it did not it would have no authority to take and use the land of individuals for the purpose of building its road. Besides, the state can, if such a policy be deemed expedient, regulate the rates for carrying passengers and freight. This could not be done if it were strictly private, like a man who might carry freight and passengers either alone or in company with other persons.

4. Lastly may be mentioned foreign corporations, actors outside the state of their creation. An insurance company created by the state of New York, but transacting business in Illinois, is regarded by the latter state as a foreign corporation.

5. Corporations are created in two ways: by general law and by a charter. The oldest way or method of creating a corporation is by legislative action. The persons who desire to form a corporation give notice before the next meeting of the legislature of their intention to apply to that body for the creation of a corporation. On assembling a petition is presented through a member, setting forth this fact or wish, accompanied by a bill setting forth the powers which they desire to have conferred on them.

The petition is referred to an appropriate committee, a report thereon is made and discussed by the respective houses, and if the bill is considered favourably and signed by the governor, the associates are endowed with corporate power. Charters are monopolies, and in olden times especially were regarded as very valuable. Their creation gave rise to many abuses; furthermore, the method was too slow for the demands

of modern business, and so another mode has been adopted for accomplishing this end more speedily and effectively.

6. This is by enacting general laws providing for the creation of corporations. In probably every state there is a law of this character, prescribing conditions on which corporations can be formed; and besides this general law, some states have also other laws providing especially for different kinds of corporations, like railroads, banks and insurance companies. These laws provide that application must first be made to officers who are named—the secretary of state, attorney-general, superintendent of banking, or other officer, or perhaps to several of them. The application is then examined, the associates give proper notice of their formation, pay in their capital, elect officers, and comply with every other legal requirement. When these things are done the corporation is born, endowed with real life. All corporations therefore created by general law of the same class or kind possess similar powers; while those chartered by the legislature are often endowed with powers more varied and extensive.

7. A corporation is often regarded as a perpetual body; of late years a shorter term has been given to them. The national banks, for example, are chartered for a period of twenty years, and many of them have had their charters renewed, and are living during the second, or even third, period of their existence. A corporation never dies in the same sense that death overtakes an individual. Its members die, others take

their places. A corporation may be likened to a river —ever changing, yet ever flowing.

8. A corporation has no heirs or inheritors like an individual; it continues through succession, one member succeeds another, like the leaves on a tree; in this way its life is preserved.

9. The authority of a corporation depends on the will of the legislature; it is a creation of the state. It has such powers as are expressed in its charter or by general law, with such incidental powers as are needful for the effective execution of these specially granted. Formerly, a corporation could not hold property for the use of another, it could not be a trustee; now, a corporation can transact such business if the authority has been properly conferred. In many of the states they often act as executors and administrators of estates.

10. A corporation has a seal; a partnership has none. Once it was said that the seal must always be used in the transaction of its business; it could not express an intention by any personal act; it had no soul, it could not speak, but only make an impression. This view of a corporation was found to be too limited; its business became too extended to be transacted in this slow manner; consequently, it was long ago declared that a corporation could make verbal contracts through its executive officers in the same manner as a partnership. How badly fettered would a railroad be if obliged to affix a corporate seal to every freight contract made by its agents. Very many things therefore may be

done to which a corporate seal need not be added to make them legal.

11. The authority or privilege conferred on a corporation is called a franchise. *Quasi* corporations have no privileges or franchises. This is one of the marks that distinguish them from other corporations.

12. Every corporation must have a name by which it is known. Corporations in the same state should not have a similar name; nor would one be intentionally granted to a second corporation.

13. Corporations can sue and be sued in the same manner as individuals. This authority and liability is prescribed by statute, and is important to their life and power. If a corporation could not sue it would be crippled in transacting its business; on the other hand, if it could not be sued it would not be safe for others to do business with it. Its liability to sue and to be sued is very general, extending to contracts, negligence, and wrongs of all kinds.

14. A corporation can hold and sell real estate. Some limits have been put on corporations in this regard. The national banking law prohibits a bank from holding more real estate than is necessary for banking purposes; it cannot even take real estate to secure a note that is discounted in the beginning, though it may do so afterward as additional security. If a complete title to such estate were acquired by proper legal proceedings it could not be held for a longer period than five years. The bank would be then obliged to sell, whatever might be the price obtainable. The reason for thus restricting corporations

in the holding of real estate is to prevent them from getting possession of too much. There was a time in English history when corporations owned such a vast quantity of real estate that a restrictive law was passed which afterward was enforced in the American colonies. Modified from time to time, corporations can now hold whatever real estate may be necessary for effectively transacting their business. For example, a railroad company can buy land for its way, for stations and offices, but it cannot buy land for ordinary investment or for speculation.

15. Once a year an annual meeting is held by the shareholders for the election of directors, and other business. At this meeting the shareholders are either present and vote, or they are represented by others; very frequently they give an authority, called a proxy, to some other person to act for them. Not infrequently an annual meeting is held at which two or three persons act for a very large number of shareholders. Usually each share is entitled to a vote, but some charters provide that each shareholder has only one vote notwithstanding the magnitude of his holdings.

16. The meeting must be held at a reasonable hour, and in a convenient place to the great body of shareholders. Generally the charter prescribes where the meeting must be held. It is said that there is no objection to holding a meeting in a foreign state, provided all the directors give their consent. Morawetz says that in the absence of an expressed statutory prohibition there appears to be no reason why the shareholders in an ordinary business corporation should not

provide in their articles of association that meetings may be called at convenient places outside the state under whose laws the company is formed.

17. The meeting is controlled by the majority. They comprise that portion of the stockholders who are present at the general meeting and entitled to control the corporation by their votes.

The majority need not be present at the meeting in order that the resolutions may be binding on the corporation. Unless there is an express statute to the contrary, the rule is that such of them as actually assemble at a properly convened meeting constitute a quorum for the transaction of business, and the majority of that quorum have the authority to represent the corporation.

The power of the majority to bind the whole body is derived from the agreement of the association. The majority, therefore, cannot represent the corporation in any transaction contrary to its chartered purpose, nor can they do anything without complying with every formality prescribed by charter, statute or custom.

The majority of the corporation can exercise no greater powers than the individual members of the company can bestow. The courts would undoubtedly scrutinise with strictness any acts of a majority who should seek to obtain an advantage at the expense or loss of the corporation as a whole. Should they attempt to appropriate the corporation's funds to their own use, or to depart from the company's charter or from the general law that governs corporations, the courts would interfere to protect a shareholder.

18. The action of the majority, even though unauthorised by the charter, may be ratified by the other shareholders. Very many informal acts are rendered valid by subsequent unanimous consent.

19. To enable the majority to act at a meeting this must be called in a proper manner. Every shareholder is entitled to be present and to have a proper notice thereof. The statutes and by-laws passed by the company prescribe how notices must be given. If a notice to anyone is omitted those present have no authority to act for the whole body, and the transactions at the meeting will not be binding as corporate acts. Says the highest tribunal of New York: it is not only a plain dictate of reason, but a rule of law that no power or function entrusted to a number of persons can be legally exercised without notice to all the members composing such a body.

If, however, the charter and by-laws of the company fix the time and place at which regular meetings shall be held, this is a sufficient notice to all the shareholders, and no further notice need be given.

If the charter and by-laws contain no express provision for calling meetings, the managers have authority to do so when they deem meetings to be desirable. In most cases the laws provide in express terms what officers shall have authority to call meetings.

20. The officers who wrongfully refuse to call a meeting as they ought to do by law may be compelled to do their duty by the courts in a proceeding called a mandamus; in other words, the courts can compel the

officers to call a meeting in obedience to the wishes and request of the stockholders.

21. A distinction has been made between regular and special meetings. The former are held in the manner prescribed in the charter and by-laws; the special ones are called at irregular times on proper authority. A notice for a special meeting must state particularly the object, and no business can be transacted except that stated in the notice.

The rule is otherwise concerning the notice of a regular meeting. Unless the business be of great importance, nothing need be said concerning it. Thus, a mutual fire insurance company held a meeting which was called for the purpose of making alterations in the by-laws, and transacting such other business as might come before the members. It was decided that the notice was not sufficiently specific to enable the majority of those present to increase the number of the directors.

22. An authorised meeting may be adjourned from time to time without giving further notice to the shareholders. This is simply a continuation of the original meeting. Says Judge Redfield: whether a meeting is continued without interruption for many days or be adjourned from day to day or from time to time, many days intervening, it is evident that it must be considered the same meeting without any loss or accumulation of powers.

23. The members may adopt reasonable by-laws regulating the manner of voting and holding meetings and directing the order of proceedings. Their validity depends on the implied agreement of all the share-

holders in forming the corporation, and therefore any by-law properly enacted by the majority is as binding on the members of the company as those provided in the charter.

24. What by-laws a company may make must depend on the charter and general statutes, as well as public policy. Not every by-law made by a corporation is valid, only those that are reasonable and needful to carry into effect the objects of the corporation. Many of the by-laws regulate the manner of holding meetings, electing officers, transferring shares, and the like.

As the charter or general constitution, either alone or combined, is the fundamental law, it cannot be set aside by adopting contrary by-laws. Nor can the authority of a corporation created by charter or statute be enlarged by a by-law. For example, a by-law would not be valid authorising a corporation to make a usurious contract. In one of the cases Justice Folger declared that "all by-laws must be reasonable and consistent with the general principles of the law of the land by which they are to be determined by the courts when a case is properly before them. A by-law may regulate or modify the constitution of a corporation, but cannot alter it. The alteration of a by-law is but the making of another upon the same matter. . . . But a by-law that will disturb a vested right is not such."[1]

25. Clearly, every by-law must be reasonable in the way of affecting all interests. Thus, a by-law of

[1] Kent v. Quicksilver Mining Co., 78 N. Y., 182.

a chamber of commerce, providing for the expulsion of a member who did not comply with a contract he had made with another member, was held valid. Clubs, benevolent societies, and other associations usually provide by-laws for trying and expelling their members who have valid obligations imposed upon them by virtue of their membership. Such by-laws have often been sustained, though it may be added that before a member can be expelled there must always be given him an opportunity to defend himself against the charges preferred against him.

By-laws that are vexatious or manifestly detrimental to the interests of the corporation are void. Thus, a majority have no authority to pass a by-law declaring that a member who fails to pay an assessment shall forfeit his share or a dividend until all arrears have been paid.

Again, a by-law requiring the members of a company to submit their controversies to arbitration, otherwise they are to be expelled should they bring suit, is invalid.

26. Banking institutions are constantly adopting new by-laws as the occasion for them arises. This is especially true in regulating the payment of deposits. It is generally said that a depositor must have a notice of a by-law in order to be bound thereby; nevertheless, he may submit to a by-law prescribing that he shall be bound by any amendment that may be made to the by-laws, even without notice of it. This rule has been applied on several occasions. Though on the very verge of the law, it has judicial sanction.

27. Sometimes savings-bank depositors have con-

tended that they were not bound because they could not read the by-laws. The courts have said that this was no excuse; that they ought to ask others to read the by-laws to them. In no case is a bank required to interpret a by-law to a depositor. In many cases there are several depositors in a bank having the same name, and it is quite impossible to identify every one of them. A very common rule among savings banks, that it deems itself justified in paying a deposit to a person who presents a book and claims to be the owner, unless there is some reason to suspect wrong-doing, will justify the institution in making payment. No rule will absolve a bank from negligence in this regard.

Again, a by-law of a savings bank prescribing the mode of investing savings-bank deposits is merely a direction to the officers of the bank, conferring no rights whatever on the depositors.

28. Companies that are engaged in a public business, like a railroad, frequently adopt and publish rules for the government of those who transact business with them. These rules, though called by-laws, are obviously somewhat different from the by-laws passed by a corporation for its own management. By-laws of the latter kind are binding by virtue of the implied terms of the contract. By-laws of the former class are merely conditions binding all persons who choose to deal with the corporation. Thus, railroad companies provide rules for transporting travellers and goods and regulating the terms of service of their own employees. Persons dealing with them who know the rules and regulations thus published are held to assent thereto.

29. Lastly, a corporation cannot enforce a by-law giving a lien of the shares of its members for debts due the company as against the bona fide purchaser of certificates of the shares who had no notice of the by-laws.

While every member is bound by the by-laws adopted by the majority, a non-member is not bound nor can he claim any right by force of a by-law. The Supreme Court of Massachusetts has declared that the office of a by-law is to regulate the conduct and to define the duties of the members toward the corporation and between themselves. So far as its provisions are in the nature of a contract the parties thereto are the members of the association themselves. The right of a third party, a stranger to the association, to establish a legal claim through such a by-law must depend on the general principles applicable to express contracts.

30. A person who deals with an agent of a corporation is not required to take notice of the company's by-laws, nor is knowledge of them presumed. Therefore a contract made in good faith with an agent of a corporation when the agent is acting within the scope of his apparent powers binds the corporation itself, although the agent acted in violation of the existing by-laws.

31. The right of vote belongs only to the shareholders. The assignees of shares that have been equitably assigned cannot vote on them until they have been formally transferred in the manner prescribed by the charter and by-laws of the company.

32. The vendor or seller of shares, therefore, and

not the vendee, can vote on them until they have been transferred on the stock books. The same rule applies between an obligor and an obligee, a mortgagor and a mortgagee. A trustee, also a guardian, can vote, so long as he is legally serving in that manner. Likewise the corporation itself holding any shares can vote on them through an agent who is duly authorised for that purpose.

33. Of course, a person may restrict his right to vote in various ways; thus, a shareholder who has made a sale of his stock has in truth no right as against his assignee to vote on them without his consent, although the regular transfer may not have been exexuted on the company's books. The rights, however, between the assignor and assignee are one thing, and the rights between a second party and the company are another.

34. The right of a trustee to vote on shares depends, it is said, on the terms of the trust. Usually, he has this authority.

35. Joint owners who disagree about voting can cast no votes.

36. To receive illegal votes will not necessarily vitiate the action of the majority. If there are enough votes to elect a director—for instance, after throwing out the illegal ones—his election is lawful; but a person who has received a minority of votes cannot be declared elected, because a sufficient number of votes in his favour to make up the majority was refused. The denial of jurisdiction in courts of equity to restrain persons from acting as officers under a void election

does not proceed from the supposed incapacity of courts of equity to pass on a question of this kind. The reason is because the legal method is clear and effective. Therefore when the object is to declare the regularity of the election or to declare the office to which one has been elected forfeited, a court of the law is a competent and proper tribunal.

37. It has been held that votes cast for a candidate who is disqualified for the office will not be thrown away, making the election fall on a candidate having a minority of votes, unless the directors cast their votes with full knowledge of the fact and consequences.

38. Stockholders often vote by proxy, but the right to do this must be expressly conferred by the company's charter or by-laws. The power of attorney to execute this authority need not be in any prescribed form nor executed with much formality. Says the Supreme Court of New Jersey: "A stockholder . . . is undoubtedly bound to furnish his agent with such written evidence of the latter's right to act for him as will reasonably insure the inspectors that the agent is acting by the authority of his principal. But the power of attorney need not be in any prescribed form nor be executed with any peculiar formality. It is sufficient that it appear on its face to confer the requisite authority and that it be free from all reasonable grounds of suspicion of its genuineness." [1]

39. A corporation cannot vote on its own shares. It is only by a fiction that they can be regarded as

[1] In re St. Lawrence Steamboat Co., 44 N. J. Law, 534.

existing. It would be an absurdity to allow the company to vote on them for the purpose of controlling or diminishing their voice in the management of their own property.

40. The right to appoint inspectors or judges of election is vested in the shareholders themselves. Neither the shareholders nor inspectors can inquire into the true ownership of the shares, or deprive a legal owner of his right to vote. Says Justice Depew, in an important opinion: "The general rule is that the books of a corporation are the evidence of the persons who are entitled to the rights and privileges of stockholders in the management of the affairs of the corporation, with the single exception that the stock really belonging to the company cannot at any election for its directors be voted on directly or indirectly." [1]

41. A corporation has implied authority to carry on its legitimate business in foreign states, unless this is prohibited by its charter. Of course, no state can authorise a corporation to engage in business outside its own jurisdiction, because if it could there would be a clash in the conflict of jurisdiction leading to the gravest results. On the other hand, the principle of comity is given wide application in permitting corporations having a legal existence in the state of its origin to do business elsewhere.

The general principle may be thus stated. A corporation in Pennsylvania, engaged in banking, manufacturing, insurance or other business, is permitted to

[1]. In re St. Lawrence Steamboat Co., 44 N. J. Law, 539.

do anything pertaining to its business in the state of New York, for example, that any corporation of a similar character can do there, not opposed to the interests or policy of the citizens of that state. If the Pennsylvania corporation wishes to buy land in another state it must conform to the law of such state in its purchase and management, because the principle prevails everywhere with regard to land that the laws that apply thereto are those strictly of the place of location.

42. In the early federal case of the Bank of Augusta v. Earle,[1] the Supreme Court of the United States considered this subject. The court said that it was very true that a corporation can have no legal existence beyond the limits of the sovereignty by which it is created. "It must dwell in the place of its creation, and cannot migrate to another sovereignty. But, although it must live and have its being in that state only, yet it does not by any means follow that its existence there will not be recognised in other places, and its residence in one state creates no insuperable objection to its power of contracting in another."

43. A corporation therefore can by its agents go into another state and make any contract or conveyance within its chartered authority, provided it is not prohibited by the laws or policy of such state. Again, it may maintain an action to enforce its rights in another state or country unless such action is contrary to its laws, very much as the corporation can do in the state of its own creation.

[1] 13 Pet., 519, 585.

44. The rules of comity have the force of legal obligation and it is the duty of the courts to respect them. Comity is a part of the common law.

45. As a state may entirely exclude a foreign corporation, it follows that it may impose a tax or license fee on a foreign corporation even if no tax is imposed on a similar corporation of its own creation. A foreign corporation may, therefore, in competing with a domestic corporation, be put at a disadvantage for which there is no remedy unless perhaps that of public retaliation.

46. Thus, a state may enact laws, and many of them have done so, regulating the mode of doing business by foreign fire and life insurance companies. Some states require foreign corporations doing business within their territory to have an agent there who can be sued, instead of requiring a policy holder to go to the state where the company exists, in order to bring a suit on the policy, in the event of failure to obtain a proper settlement.

Again, some states require a foreign insurance company to have a fund within its territory, so that it may always be able to respond to the demands of claimants. Such regulations are not at all uncommon, nor do they infringe particularly on the general principle above noted.

47. A state cannot prevent a corporation from removing a suit into the federal courts; and a stipulation to that effect as a condition of its permission to do business would be void.

48. A board of directors may hold their meetings

outside the state where their company is chartered, unless the by-laws or charter forbids such action.

§ 3. Directors and Managers

1. Directors are shareholders.
2. Disqualified director has no authority.
3. They should possess business experience.
4. Their general authority.
5. How far it extends.
6. Directors can act only as a board.
7. Can ratify separately.
8. They cannot expel a director.
9. Are not technical trustees.
10. Must pay their company's debts, regardless of consequences.
11. Cannot fix their own compensation.
12. Cannot make a valid contract with themselves.
13. By the modern law their contract is voidable.
14. Majority can safely contract with one or more of their members.
15. Directors may contract with shareholders.
16. Imputation of director's knowledge to his company:
    a.—Reason for rule,
    b.—Difficulty in applying it,
    c.—When it is not imputed.
17. Action of same directors in two companies with opposing interests.
18. General liability of directors; minimum rule.
19. Maximum rule.
20. Are liable for false representations.

21. What must be shown to maintain action.
22. Directors may resign:
    a.—How this should be done,
    b.—Do not escape previous liability by resigning,
    c.—When they cannot resign.
23. Distinction between their business and ministerial duties.
24. Authority of general officers.
25. Extension of their authority.
26. A bank president.
27. Extension of authority is not uniform.
28. Gradual growth of authority.
29. Authority of vice-president.
30. Appointment and authority of agents.
31. Officer is as responsible to his company for wrong-doing as to a stranger.
32. Remedy.
33. Liability of officers to creditors and stockholders for wrong-doing.

1. A corporation is governed by the directors, who in turn are guided by its charter the general statutes and the common law. The directors are always shareholders unless the company's charter contains a provision to the contrary. The National Banking Act requires that every director shall own at least ten shares of stock, and somewhat similar provisions exist in the laws regarding other corporations. But a director who becomes bankrupt does not thereby vacate his office.

2. The majority of a corporation cannot elect a person to the office of director who is ineligible by the terms of the charter, and a person who is not qualified to act as a director has no authority to represent the corporation.

3. The directors should be men of practical business judgment, and selected by reason of their fitness to manage the corporate affairs. It does not follow that the majority of the shareholders can control them, or interfere with their management. The authority of the board is derived from the unanimous agreement of the shareholders expressed in its charter, and hence their power cannot be impaired by the majority. Says Morawetz: "The rule limiting the authority of the power of the majority to the general supervision of the affairs of the corporation is established for the protection of the individual shareholders, as well as for reasons of practical convenience. A board of directors selected by the shareholders are better adapted to carry on the business of the company successfully than the shareholders themselves assembled at a general meeting."[1]

4. The general authority of the board extends to the management of the regular business of the incorporation. Even an express provision that the powers shall be exercised by its board of directors does not deprive the majority of the shareholders from directing the general policy of the corporation, and of deciding on the propriety of important changes in the company's business. Says Morawetz:[2] "The board

[1] § 511.
[2] § 239 (First Edition).

of directors has no implied authority to make a permanent change of the business or constitution of a corporation, even though the alterations be within the company's chartered powers. Such an alteration can be effected only by the shareholders at the general meeting. For the same reason the directors cannot wind up the company, or sell any property which is necessary to the company's business."

5. How far their authority extends depends on the company's charter and statute. No agent under any circumstances can act in violation of law. The authority of the president and directors of many companies is largely determined by custom, and parties who deal with them are supposed to be familiar with their authority.

Furthermore, directors have wide discretion in delegating their authority. How far they can go depends on their charter, by-laws and usage. In many corporations the tendency is for directors to circumscribe more and more their work and appoint others to assist them.

A very good illustration of this is furnished by the action of bank directors in delegating their authority to lend the bank's money to the president, the cashier or a committee. There was a time when this could not be done. The law was very strict in maintaining that this was the chief duty of the directors, and must actually be performed by them. By the modern law, except in a few states, they may delegate their entire authority, even in this most important matter, to a committee of their board or two or three officials of the bank.

Thus, the specific powers and duties of the directors

are constantly narrowing. There are, however, some duties which they cannot delegate to others. For example, the making of the reports required by statute.

6. A director has no authority to act separately and independently of his fellow members. Only as a board, duly convened, is he a representative of the corporation.

If, therefore, each one should separately, outside a board meeting, assent to an act it would not be a corporate act and binding on the company.

It is not necessary for them all to meet, and rarely do they all, especially the members of a large board, but notice of their meetings must be properly given, and the majority when assembled must act in the manner prescribed by the statute and by-laws.

7. While it is true that directors can act only as a board in performing their duties, they can singly ratify the action of their officers, and in this way a great many acts are legalised. On many occasions only a small number of the directors attend, and yet, generally speaking, all, with few exceptions, have a good knowledge of the most important affairs at least of their corporation. Their knowledge, by whatever method acquiried, operates as an acquiescence in or ratification of what has been done. This principle of ratification plays an important part in the management or conduct of nearly all corporations.

8. It is a general law of agency that the powers of an agent may be revoked at any time by his principal. The rule does not apply to corporation directors.

Says Morawetz: "The majority of the board clearly have no power to expel an individual director, or to exclude him from inspecting the company's books and participating in its management, although they may believe him to be hostile to the interests of the association."[1] Though they may have no authority to revoke the powers of any agent, like a president, or treasurer, whose term of office is fixed by the charter or articles of association of the company, it does not follow that they have authority to remove an agent of this character merely because they appoint him pursuant to the provisions of the charter. There should be an express provision granting the power of removal.

9. The directors are not trustees in the technical sense, though they are often thus called. Yet the relation between the directors and the company is in many respects a trust relation. Whenever, therefore, an agent is invested with authority to use any discretion this must be exercised in good faith for the benefit of his principal.

10. It is their duty to pay the company's debts, and they are justified in using the corporate assets for this purpose, although the company be thereby disabled from carrying on its business, provided they act in good faith and with due regard to the interests of all the shareholders.

11. The directors of a corporation cannot fix their own compensation. They are entitled to none for their official services unless this is provided by charter or by-law, or by the shareholders. But a director who

[1] § 541.

is employed to perform other services—an attorney, for example—can charge for this.

12. Directors have no right to bind the company by any contract made with themselves personally, or to represent it in transactions with a third party wherein they have a private interest. This is founded on the general principle of agency that an agent cannot act at the same time for both parties. Yet this principle is constantly violated. Thus, on one occasion the shareholders of a company empowered the directors to obtain a loan of money for the purpose of carrying on the company's business. Instead of honestly executing the order the directors borrowed fifteen thousand dollars and used the larger portion in paying their own debts. The court held that this was an unauthorised transaction. Said Justice Davis: "Directors hold a place of trust and by accepting it are obliged to execute it with fidelity not for their own benefit but for the benefit of the stockholders of the corporation."

Again and again it has been decided that a director cannot become the purchaser of property sold at public sale.

13. To this rule there is an important qualification. The transactions between directors and their companies are not necessarily void, but simply voidable. Many of them are made in perfectly good faith and for the best interests of the company. In making them the directors seek no undue or wrongful advantage. In every case of this kind the law declares that the company may set aside such transaction at any time before

the statute of limitations has gone into effect. But corporate life now plays such an important part in the business of the world that it has become needful to modify the rule as above expressed.

14. Another principle has also come into operation within a comparatively recent period. A majority of the directors of a corporation may lawfully act as opposed to the minority and this rule rests on reasonable ground. For, so long as the majority of the directors are acting for the corporation, their action is in a true sense the act of the corporation itself. Thus, suppose a single director of a bank wished to borrow money and made a proper application therefor, and the remainder of the board should act favourably on his application, such action would be unquestionably legal, as clearly as if he were an outsider.

We may readily imagine a different state of affairs. Suppose a director should make an application on which all the others should act, by agreement, favourably. Clearly there would be in form two parties to the proceedings. Suppose each director in turn should make a similar application on which the others should act in the same manner. Though in form there would be two parties in each transaction, yet in reality there would be only one, as each loan would rest, after all, on the prior agreement or understanding. The law in such a case would look at the real agreement or conspiracy among the directors, and not at the form or shell in which they might express their action.

15. Directors and shareholders may deal with each

other as freely as with strangers. There is no trust relation between directors and shareholders except in the management of the corporate interests.

16. The knowledge of a director or other officer of a company is said to be imputed to it under many conditions or circumstances. It is true that this rule is less effective than formerly, because it is somewhat artificial in its nature.

(*a*) Nevertheless, it is founded on a sound basis, that the knowledge of an agent is presumed in law to be the knowledge of his principal, who is affected thereby.

(*b*) The difficulty with the principle in practical operation is, the agent does not always communicate the knowledge; consequently the principal in fact does not always possess the same knowledge of the transaction as the agent himself. The tendency of the modern courts, therefore, which have a deepening regard for justice, is to narrow the operation of this great principle.

(*c*) Thus, in the conduct of a director there are many exceptions to the operation of this principle. It is said, for example, that if knowledge is acquired by him in the ordinary way it is often not to be imputed to his corporation for the reason that he is a business man more deeply interested in his own affairs; and that it is not quite fair to assume that he will charge his mind with the knowledge thus acquired and communicate it to his company. Suppose a director learns about some defect in a note, the ability of the payee or indorser, and that it is presented for discount at a

meeting of his bank attended by himself. His knowledge of its imperfect character is not imputed to the bank for the reason that the law does not assume that he has retained the information accidentally acquired. So, too, knowledge that he may have acquired before becoming a director or in outside operations and ways are not chargeable to the bank. In short, to impute the knowledge acquired by him to the bank, he must be specially charged with the duty of communicating it. If he should be told something and promise to make the information known to his associates, and forget or neglect to comply, then the bank or corporation would be regarded as having the notice.

On one occasion it was remarked that "a notice to a bank director or trustee, or knowledge obtained by him while not engaged either officially or as an agent or attorney in the business of the bank, is inoperative as a notice to the bank." If this were not the law "corporations would incur the same liability for the unofficial acts of directors that partnerships do for the acts of partners; and corporate business would be subjected oftentimes to extraordinary confusion and hazards. Any director would have as much power as all the directors. A single trustee or director has no power to act for the institution that creates his office except in conjunction with others."

17. Persons who are appointed to act as directors of different companies have no authority to represent them in transactions wherein their interests are opposed. Nor does it matter whether the acts of the directors are in the interests of the majority of the

shareholders of each company and have received their approval. Says an authority from whom we have already quoted, nothing can be more unjustifiable and dishonourable than an attempt on the part of those holding the majority of the shares of a corporation to place their nominee in control of the company and then to use their control for the purpose of obtaining advantages to themselves at the expense of the minority. It would be a conspiracy to commit a breach of trust.

In one of the cases calling for the application of this principle two railroad companies, whose lines connected with a third company, bought a controlling interest in its stock and elected a number of their own agents directors. They proceeded at once to make contracts between this company and the other two which were injurious to the minority interest of the third company. The Supreme Court of New Hampshire, where this contention arose, held that the third company whose management had thus been changed had an absolute right to refuse to be bound by the transactions, whether the contract was fair or not.

This principle is far reaching and most salutary. The cases are constantly occurring in which the majority in interest take advantage of their position to wrong or injure the minority interests, and the courts need to be vigilant in thus guarding the interests of the minority against raids made by those who are in control.

18. The liability of directors is not so great as many suppose. Directors are advisers and not managers, and

are not responsible for much that pertains to the management of their association. They are responsible for fraudulent conduct and for specific violations of positive law, but not for mistakes. Two rules apply to their acts of negligence: these we may call the minimum and maximum rules. By the minimum rule a director must exercise ordinary care and attention. Suppose a bank director should neglect to attend the usual board meetings, and the other directors should make loans exceeding the amount prescribed by law, would the absenting member be guilty like the others? If he knew or suspected that they were violating the law, and intentionally remained away, by some tribunals he would be regarded guilty for not attending and attempting to restrain his co-directors, or, if failing in his good purpose, for not resigning. But, ordinarily, he is not required to attend, regularly, board meetings, and if he remained away, not knowing nor suspecting that his co-directors were violating the law he would not be responsible for their wrongdoings.

19. By the maximum rule directors must exercise the same degree of attention in conducting the business of their corporation that prudent men exercise in conducting their own affairs. In a recent case the court thus stated the rule: "It is necessary for them to give the business under their care such attention as an ordinarily discreet man would give to his own concerns under similar circumstances, and it is therefore incumbent upon them to devote so much of their time to their trust as is necessary to familiarise them with the busi-

ness of the institution and to supervise and direct its operations." [1]

The minimum rule has the sanction of the highest federal tribunal, and also of the supreme courts of a few states; the maximum rule has the sanction of far more.[2]

20. Directors are responsible for false representations concerning the funds of their company whereby others are induced to give it credit or to purchase its obligations or shares. When they issue reports or a prospectus intended for general circulation and to advertise and give credit to the company with the public, they are responsible for the natural consequences of their action, and if the report or prospectus were false or fraudulently made, any one who is misled thereby has an action against the directors. This principle has been applied on many occasions.

In one of these cases, which has often been cited, the directors were promotors of a mining company, and a purchaser, by their false statements, was led to believe that the company owned a large amount of property. Relying on them, he purchased shares in the company, which proved to be worthless. He had the satisfaction though of recovering from them his loss.

21. To maintain this action it must be shown that their representations were false and made wilfully. They are assumed to have general knowledge of the company's management and financial condition. Knowing that their position naturally leads the public to

[1] Warren v. Robinson, 19 Utah, 289, 303.
[2] See article by the writer in March No. of Yale Law Journal, 1903, for a full exposition of the law on this subject.

believe their statement, it is their duty not to abuse this belief by false or thoughtless statements. Yet they are not presumed to have notice of everything relating to the management and organisation of the company; only those things which would be necessarily known to them in the performance of their office. They are not liable for publishing reports in good faith based on dealings furnished by the ordinary managers and clerks whom they employ.

22. Directors when accepting office impliedly agree to retain them until the next election. They may, though, at any time resign.

(*a*) Those who wish to terminate their liability by resigning should express their wish in an orderly manner, so that new directors may be elected.

(*b*) They cannot escape from a liability already incurred by ending their relationship; they are also chargeable for losses afterward resulting from any breach of duty previously committed. In one of the cases it was held that a director who had resigned could not be held liable under the statute rendering the directors liable for failure to file annual reports, although the resignation had not been accepted and entered on the minutes of the corporation.

(*c*) Again, they cannot terminate their agency or accept the resignation of others when such action would leave the company without proper care and protection.

23. A distinction has been made between the obligation of directors to act as agents or business managers of a corporation and their obligation to perform those

ministerial duties which are necessary to perpetuate the corporate organisation. They cannot divest themselves of their legal status as part of the corporate organisation save in the manner prescribed by law. If their term of office is fixed by the charter at a defined period they continue legally to be officers of the company, and are bound to call meetings and to do such other ministerial acts as are necessary to protect the company until their term of office has expired or their resignation has been properly accepted.

24. The authority of the president and other general officers will now be considered. Their authority is defined either by statute or charter or by the common law. Whenever specific duties and liabilities are prescribed in this way they have authority to act within the scope and usages of the business to which their conduct relates, and are liable if they exceed them. Thus, if a person is a general agent of an insurance company, he has authority to transact the business falling within the limits of such general agency. In other words, he can go as far in binding his company by his acts as the agent of an unincorporated principal. As the United States Supreme Court has remarked, "Corporations are liable for the acts of their servants while engaged in the business of their employment in the same manner and to the same extent that individuals are liable under the same circumstances." A cashier of a bank, therefore, would bind his institution by his acts so far as they were within the scope or usage of the business, even if in doing so he violated his private instructions. If, for example, he had no

authority to certify a check beyond the maker's deposit, and should do so, the bank would be bound by his act, because it is within the scope of his authority to certify checks. A corporation can act through an attorney like an individual.

25. The tendency of the times is to endow the general officers of a corporation with more authority than they once possessed; in other words, to enlarge the general scope of their authority. This is because the old feeling of prejudice and fear concerning corporations has diminished, and their efficiency often consists in endowing their leading officers especially with greater authority.

26. Within a few years the authority of a bank president has been enormously enlarged with judicial sanction. Formerly it was of the most limited character, but his efficiency as a manager and the requirements of modern business both unite in endowing him with the most general authority. In the large cities especially the president is usually the real head, and is responsible for the conduct of the bank's business. In a recent case Judge Hawley thus concisely expressed the authority now vested in such an officer: "It is now well settled by the weight of reason and authority that whenever in the usual course of the business of a corporation the president or other officer has been allowed to manage and control its affairs, his authority to represent and bind the corporation may be implied from the manner in which he has been permitted by the trustees or directors of the corporation to transact its business. The acting head of a corporation,

whether it be the president, vice-president, cashier or general manager, through whom and by whom the general affairs of the corporation are transacted which custom or necessity has imposed upon the officers—such acts being incident to the execution of the trust imposed in him—may perform them without express authority, and in such cases it is immaterial whether such authority exists by virtue of his office, or is imposed by the course of business as conducted by the corporation."[1]

27. It is true that he does not possess as much authority everywhere, nor under all conditions. In many of the country banks the cashier is still the real head, and the president is clothed with no more authority than he had formerly. When, therefore, this question arises it must be determined by statute and usage or custom. But the strong tendency is to clothe the president with more authority by reason of the fact that he has become manager. But where he is merely a nominal officer his authority is no greater than in the earlier day.

28. There is a peculiar class of cases in which the authority confided in a company's officers may be gradually extended. Thus, a man when appointed to a given position may be very young and the directors are unwilling to confide much authority in him. As he grows older and becomes more efficient his authority is enlarged until, after several years, perhaps, it is practically unlimited. A change is therefore gradually going on from the time of his beginning until the

[1] Cox v. Robinson, 48 U. S. App., 388, 400.

complete extension of his authority. In these cases, which are quite numerous, the authority under which a person acts in performing a given thing must be largely a matter of inquiry. This is especially so with regard to all acts that are outside of the clear lines of his general authority.

29. It is often said that the vice-president takes the place of the president during his absence, and is clothed with his authority. When the by-laws specially state that, in the absence of the president he is to exercise his powers, then, unless the by-laws contravene a fundamental law, he doubtless can act in every respect in the president's place; but usually the by-laws do not confer on him as much authority, and there are very good reasons for withholding it, as he often possesses less ability and knowledge of the company's business.

30. Corporation agents may be appointed in the same manner as agents for an individual. No formalities are required nor need a corporate seal be used unless required by charter.

The appointment does not go into effect until acceptance by the appointee. This may be presumed from the exercise of the power conferred, or from acquiescence with knowledge of the resolution of appointment.

Again, a person who is allowed to act as an agent with the knowledge of a superior agent who would have authority to appoint him, thereby binds the corporation, and it cannot thereafter repudiate his agency.

The authority of lesser agents often depends upon

custom and modes of dealing with the company. Thus, the secretary and treasurer of a company may have no authority by virtue of his office to sell corporate property; yet he may be invested therewith by specific authority by a course of dealing.

31. Every officer is bound to serve his company faithfully and is as liable for wrongs committed against it as to a stranger under similar circumstances. If, therefore, he is guilty of an unauthorised act, or misapplies the corporate property, the corporation may hold him responsible for the wrong.

32. The remedy usually is an action at common law for damages. Sometimes the remedy must be in equity. Again, the corporation may treat the transaction as binding and charge the officer for the profits received, or it may repudiate the contract and proceed against him accordingly.

33. Sometimes the officers of a corporation wrongfully deal with its property, whereby the interests of creditors and stockholders are seriously injured. Then they may maintain a bill against the company and its officers for such relief as the case may require. If, for example, the officers have voted large salaries to themselves and are absorbing all the profits of the company, the court may grant relief. There was a time when it was very difficult for stockholders to obtain relief except by electing new directors, who in turn would elect new officers; this method has proved to be too slow and ineffectual. As the officers might ruin a corporation before electing others, the courts now, on the making out of a proper case, will grant more

speedy relief. The stockholders or creditors must show that they have applied to the officers to correct the evils of mismanagement, and that they have failed to do anything to lay a proper foundation for granting direct relief. The officers are clearly liable for their wrongful acts to individuals, for the conversion of property or injury thereto. Thus, any agent who should convert, lose or destroy property deposited with a company for safekeeping as a pledge, would be liable therefor to the owner. His liability is entirely independent of any which the company may have incurred. If it should contract to keep the property safely it would be liable to the owner for a breach of this contract; if an officer should do wrong with respect to it while acting within the scope of his employment it would be liable for his wrongful conduct. On a similar principle officers of a corporation who knowingly participate in any misapplication of a fund held by their corporation in trust are liable to the beneficiaries.

An officer is not liable to persons dealing with him in his representative capacity unless he is guilty of fraud. But if he should induce parties to contract with him by falsely representing the extent of his powers, or by falsely representing the existence of facts from which his authority to make a contract would be inferred, he would be liable.